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In The
Supreme Court of the United States

HARRISON CENTRAL APPRAISAL DISTRICT,

Petitioner,

v.

THE PEOPLES GAS, LIGHT AND COKE COMPANY,

Respondent.

On Petition For A Writ Of Certiorari To The Texas Court Of Appeals, Sixth Appellate District

PETITION FOR A WRIT OF CERTIORARI

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QUESTION PRESENTED

Whether the dormant Commerce Clause prohibits a State from imposing a generally applicable, nondiscriminatory ad valorem tax on natural gas stored in the State but connected to an interstate pipeline system for out-of-state transport.

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PETITION FOR A WRIT OF CERTIORARI

The Texas court of appeals held a generally applicable, nondiscriminatory state ad valorem tax to be unconstitutional, as applied to natural gas in storage on an interstate pipeline system. App., *infra*, 22. On virtually identical facts the Supreme Court of Oklahoma, "unpersuaded by [the Texas] court's reasoning," held such a tax to be constitutional. *In re Assessment of Personal Prop. Taxes Against Mo. Gas Energy*, 234 P.3d 938, 959 n.84 (Okla. 2008), *cert. denied*, 130 S. Ct. 1685 (2010). Before denying certiorari in *Missouri Gas*, this Court invited the Solicitor General to express the views of the United States. The Solicitor General advised the Court that the Oklahoma Supreme Court had reached the right result on the constitutional merits and the conflicting decision of the Texas court was therefore wrong:

> The Oklahoma Supreme Court correctly held that, under this Court's modern dormant Commerce Clause jurisprudence, petitioner had failed to establish the unconstitutionality of applying the State's ad valorem tax on personal property to stored natural gas.

Br. for U.S. (No. 08-1458), at 9.

Now that the Texas court's decision is final, this Court should grant certiorari, resolve the conflict between the decision below and the decision of the Supreme Court of Oklahoma, and reach the same conclusion on the merits that the Solicitor General did in *Missouri Gas*.

OPINIONS BELOW

The opinion of the state court of appeals (App., *infra*, 1-22) is reported at *Peoples Gas, Light, and Coke Co. v. Harrison Cent. Appraisal Dist.*, 270 S.W.3d 208 (Tex. App. – Texarkana 2008, pet. denied). The state trial court issued findings of fact and conclusions of law (App., *infra*, 25-45), which are unreported.

JURISDICTION

The judgment of the Texas Sixth District Court of Appeals (App., *infra*, 23-24) was entered on September 24, 2008. The Supreme Court of Texas denied review of that judgment on March 12, 2010 (App., *infra*, 48), and denied rehearing on October 1, 2010 (App., *infra*, 49). The jurisdiction of this Court rests on 28 U.S.C. § 1257(a).

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

The Commerce Clause provides: "The Congress shall have power . . . [t]o regulate Commerce with foreign Nations, and among the several States, and with the Indian Tribes." U.S. Const., Art. I, § 8, cl. 3.

Section 11.01 of the Texas Tax Code provides:

> (a) All real and tangible personal property that this state has jurisdiction to tax is taxable unless exempt by law.
>
> (b) This state has jurisdiction to tax real property if located in this state.
>
> (c) This state has jurisdiction to tax tangible personal property if the property is:
>
> > (1) located in this state for longer than a temporary period;
> >
> > (2) temporarily located outside this state and the owner resides in this state; or
> >
> > (3) used continually, whether regularly or irregularly, in this state.
>
> (d) Tangible personal property that is operated or located exclusively outside this state during the year preceding the tax year and on January 1 of the tax year is not taxable in this state.

Tex. Tax Code § 11.01.

STATEMENT

Like the *Missouri Gas* case, "[t]his case involves a State's taxation of natural gas stored in underground facilities located in the State and connected to a pipeline system for interstate transport." Br. for U.S.

(No. 08-1458), at 1. The narrow constitutional question presented in both cases is the same: whether the dormant Commerce Clause prohibits a State from imposing a generally applicable, nondiscriminatory ad valorem tax on natural gas stored in the State but connected to an interstate pipeline system for out-of-state transport.

There is no material difference between this case and *Missouri Gas*. Yet the Texas and Oklahoma courts employed differing analyses and therefore reached conflicting results in resolving the same constitutional question. The explanation for this confusion is that gaps remain in this Court's modern dormant Commerce Clause jurisprudence. This case affords the Court the opportunity to resolve the direct conflict between Texas and Oklahoma, and also address a broader set of continuing constitutional controversies that are of immense practical and jurisprudential importance.

A. Factual Background

The Solicitor General recited the underlying facts of the *Missouri Gas* case in her invited amicus brief. *See* Br. for U.S. (No. 08-1458), at 1-4. Those facts are materially indistinguishable from the facts of this case.

Respondent The Peoples Gas, Light and Coke Company (Peoples) is a natural gas distribution company that purchases gas from shippers on a FERC-regulated interstate natural gas pipeline

system operated by Natural Gas Pipeline Company of America (Pipeline).[1] RR 2:63, 66-67, 69, 77. Peoples ultimately sells the gas to consumers in Chicago. RR 2:63.

As part of its system, Pipeline operates a large underground storage facility in North Lansing, Harrison County, Texas, one of several Pipeline storage facilities. RR 2:30, 72, 169. A storage facility is not part of the interstate pipeline; it is a facility connected to the pipeline. *Id.* Pipeline's storage facilities allow customers such as respondent Peoples to purchase natural gas during the summer (when demand is low and the gas is less expensive) and have it stored until delivery to consumers during the winter (when demand is high and the gas is more expensive). RR 2:32-33, 73, 105-06; 4:48. To put natural gas into the underground storage facility, one must remove it from the pipeline and inject it with compressors. RR 3:13-14.

In conformity with the mandate of the Texas Constitution that "[a]ll real property and tangible personal property in this State . . . shall be taxed in proportion to its value," Tex. Const., Art. VIII, § 1(b), the Texas Tax Code authorizes ad valorem taxation of

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[1] Because this case was tried in Texas, the record appears in two distinct formats. The Reporter's Record (cited as "RR [volume]:[page]") consists of the transcript of the trial court proceedings and trial exhibits. The Clerk's Record (cited as "CR [volume]:[page]") consists of the pleadings, orders, and other documents filed in the case. "PX" stands for "Plaintiff's Exhibit."

real and tangible personal property in the State. Tex. Tax Code § 11.01(a). Section 11.01(a) does not discriminate between goods in intrastate and interstate commerce, but applies generally to all non-exempt goods that the State has jurisdiction to tax. *Id.*

Pursuant to § 11.01(a), Pipeline pays ad valorem taxes to local taxing authorities on its so-called *cushion gas* in North Lansing. RR 2:29-30, 174; 4:17. Cushion gas must remain in the storage facility to provide the necessary pressure so that *working gas* may be delivered to the pipeline. *Id.* Working gas is the balance of the gas in the storage facility that is ultimately removed from storage for transport and delivery to consumers. *Id.*

Pipeline never takes title to working gas while that gas is in the pipeline system. RR 2:175. Pipeline's customers (including Peoples) own the volumes of working gas on the system. RR 2:174; 4:27. If a storage customer "nominates" a volume of gas to be delivered out of its storage account, Pipeline delivers it pursuant to contract. RR 2:175.

For tax years 2003-2005, petitioner Harrison Central Appraisal District included on the tax rolls Peoples' allocable share (as well as the allocable shares of other owners) of the working gas balance of the natural gas stored at North Lansing. RR 3:28, 154-55, 159; PX 1, 4, 7. The allocation was based on Pipeline's records. RR 3:155. Those records included invoices showing the quantity of gas that Peoples had

in storage with Pipeline, systemwide, during the years in question. RR 2:104.

B. Proceedings Below

Peoples protested the Appraisal District's assessments of its working gas. PX 2, 5, 8. After a bench trial, a state trial court entered a judgment that the Appraisal District has the authority to assess the working gas. App., *infra*, 44-45, 46.

The Texas Sixth District Court of Appeals reversed that judgment. App., *infra,* 23. The court rejected Peoples' argument that it did not own the volumes of gas allocated to it for tax purposes. *Id.*, at 5-9. But the court accepted Peoples' argument that the Commerce Clause shields Peoples' gas from state taxation. *Id.*, at 10-22.

One month later, the Supreme Court of Oklahoma issued a contrary decision on materially indistinguishable facts and stated that it was "unpersuaded by [the Texas] court's reasoning." *Missouri Gas,* 234 P.3d, at 959 n.84.

The Supreme Court of Texas denied discretionary review of the decision below. That denial presents this Court with a direct conflict on an important, recurring question of constitutional law between a reviewable decision, which the highest court of Texas has declined to disturb, and a decision of the highest court of Oklahoma.

REASONS FOR GRANTING THE PETITION

This Court should grant the petition to resolve the conflicting responses of Texas and Oklahoma courts to the same constitutional question. The Texas court below held that the Commerce Clause *prohibits* state ad valorem taxation of natural gas in storage on an interstate pipeline system. App., *infra*, 22. The Supreme Court of Oklahoma held that the Commerce Clause *permits* such a tax. *Missouri Gas*, 234 P.3d, at 959 n.84. That conflict means that natural gas on an interstate pipeline system is taxable by state authorities if it is in storage in Oklahoma, but not if it is in storage in neighboring Texas.

The Texas and Oklahoma courts reached those conflicting results because they employed differing constitutional analyses. They did so because, in the context of state ad valorem taxation of goods in interstate commerce, it remains unclear whether or to what extent the four-pronged test this Court adopted in *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 279 (1977), is affected by other, older aspects of this Court's Commerce Clause jurisprudence.

"The Commerce Clause is an express grant of power to Congress to 'regulate Commerce . . . among the several States.'" *United States v. Int'l Bus. Machines Corp.*, 517 U.S. 843, 852 n.2 (1996) (citing U.S. Const., Art. I, § 8, cl. 3). "It does not expressly prohibit the States from doing anything. . . ." *Id.* Yet this Court has long held that "the Commerce Clause is more than an affirmative grant of power; it has a

negative sweep as well." *Quill Corp. v. North Dakota*, 504 U.S. 298, 309 (1992) (citing *Gibbons v. Ogden*, 22 U.S. (9 Wheat.) 1, 231-32, 239 (1824) (Johnson, J., concurring)). This so-called "negative" or "dormant" Commerce Clause, *id.*, "limits the power of the States to erect barriers against interstate trade." *Lewis v. BT Inv. Managers, Inc.*, 447 U.S. 27, 35 (1980).

This Court's interpretation of the dormant Commerce Clause "has evolved substantially over the years, particularly as that Clause concerns limitations on state taxation powers." *Quill*, 504 U.S., at 309. In 1977, the Court issued its watershed decision in *Complete Auto*, 430 U.S., at 274. The Court noted that in prior cases it had already "rejected the proposition that interstate commerce is immune from state taxation." *Id.*, at 288. Because "'[i]t was not the purpose of the commerce clause to relieve those engaged in interstate commerce from their just share of state tax burden even though it increases the cost of doing business,'" *id.*, at 279 (quoting *Western Live Stock v. Bureau of Revenue*, 303 U.S. 250, 254 (1938)), the Court adopted a new, four-pronged test for state taxes on those engaged in interstate commerce. A state tax survives a Commerce Clause challenge if it "[1] is applied to an activity with a substantial nexus with the taxing State, [2] is fairly apportioned, [3] does not discriminate against interstate commerce, and [4] is fairly related to the services provided by the State." *Id.*

Although that four-pronged test has provided a greater measure of predictability to modern dormant

Commerce Clause analysis, unanswered questions remain. First, as the Solicitor General observed, there remains a question regarding the continuing applicability of the Court's "continuity of transit" cases such as *Minnesota v. Blasius*, 290 U.S. 1, 9-12 (1933):

> This Court has not yet decided whether or to what extent *Complete Auto* displaces the older line of "continuity of transit" cases in the specific context of state ad valorem taxes on goods temporarily held in storage during the course of interstate transport.

Br. for U.S. (No. 08-1458) at 10. Second, there remains a question as to whether a "physical-presence" rule, which the Court has held remains applicable in analyzing Commerce Clause challenges to state *sales* and *use* taxation, *Quill*, 504 U.S., at 312-14, likewise applies to ad valorem *property* taxation.

The Supreme Court of Oklahoma in *Missouri Gas* held that both aspects of this Court's older cases were inapplicable. The Texas court below, by contrast, held that they were crucial to the analysis. Those courts' conflicting interpretations of this Court's jurisprudence resulted in their conflicting answers to the same constitutional question.

This Court should grant the petition because, as demonstrated below, the narrow constitutional question presented and the two broader constitutional controversies out of which that question arises are of immense practical and jurisprudential importance, and they are recurring. Moreover, the

decision below is erroneous. The Solicitor General so concluded when she determined that the Oklahoma court, not the Texas court, correctly resolved the constitutional issue presented. *See* Br. for U.S. (No. 08-1458), at 9. This Court should reach the same result here.

I. The Constitutional Question Presented is Important to State Taxing Authorities and Industry Participants Alike.

A. Whether Natural Gas in Storage on an Interstate Pipeline is Immune from State Taxation is Important and Recurring.

The narrow constitutional question presented in this case is the same as the question presented in *Missouri Gas*: whether the dormant Commerce Clause prohibits a State from imposing a generally applicable, nondiscriminatory ad valorem tax on natural gas stored in the State but connected to an interstate pipeline system for out-of-state transport. That this question is important is evident from this Court's invitation to the Solicitor General in *Missouri Gas* to express the views of the United States on the question. *See* Br. for U.S. (No. 08-1458), at 1. That the Solicitor General ultimately concluded that the Supreme Court of Oklahoma reached the right result for the right reasons underscores why the conflicting decision by the Texas court in this case should be reversed.

Not only is the constitutionality of subjecting natural gas in storage to state property taxation important to this Court's dormant Commerce Clause jurisprudence, but the Court's answer will have enormous practical consequences. According to the American Petroleum Institute, natural gas is a $385 billion industry in this country.[2] FERC-regulated interstate natural gas pipelines move nearly a quarter of the nation's energy long distances to markets in the 48 contiguous states.[3] Storage of natural gas on the interstate pipeline system is an important and integral feature of the system. At the close of 2007, 400 underground natural gas storage sites were operational in the United States.[4]

Storage affords great benefit to shippers. It allows them to practice price arbitrage by purchasing natural gas during the summer (when demand is low and the gas is less expensive) and having it stored until delivery to consumers during the winter (when demand is high and the gas is more expensive). RR 2:32-33, 73, 105-06; 4:48.

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[2] Am. Petroleum Inst., *Natural Gas Is America's New Frontier* 1 (2010), http://www.api.org/aboutoilgas/NATGAS_111610.pdf.

[3] Fed. Energy Regulatory Comm'n, *An Interstate Natural Gas Facility on My Land? What Do I Need to Know?* 2 (2010), http://ferc.gov/for-citizens/citizen-guides/citz-guide-gas.pdf.

[4] U.S. Energy Information Admin., Independent Statistics and Analysis, About U.S. Natural Gas Pipelines, Underground Natural Gas Storage, Underground Storage by U.S. Region, http://www.eia.doe.gov/pub/oil_gas/natural_gas/analysis_publications/ngpipeline/undrgrnd_storage.html (last visited Dec. 27, 2010).

The sheer volumes involved are tremendous. The single pipeline company involved in this case has approximately 250 *billion* cubic feet of storage available systemwide. RR 2:163. Thus, whether natural gas in storage on an interstate pipeline system is subject to state property taxation (as the Supreme Court of Oklahoma held and the Solicitor General agreed), or is constitutionally immune from such taxation (as the Texas court held), is of considerable practical importance both to industry participants (which can at least pass along costs to their ratepayers) and to cash-strapped state and local governments.

The recurring nature of this constitutional issue is evident from its coming before this Court twice within a short period of time – first in *Missouri Gas* and then in this case. The nature of the conflicting decisions virtually ensures that the issue will further recur. Any State that has a natural gas storage facility will be encouraged by the Oklahoma decision to tax the working gas stored in that facility. Any taxpayer that faces such taxation will be encouraged by the Texas decision to contest the tax. No state court will be confident as to which analysis is correct unless and until this Court addresses it.

Industry participants have recognized that the issue is recurring and should be addressed by this Court. In its amicus brief to this Court in the *Missouri Gas* case, the American Gas Association stated: "The *ad valorem* taxation of natural gas in FERC-regulated storage within the interstate transportation system presents a recurring issue that merits this Court's attention." AGA Amicus Br. (No.

08-1458), at 3. Because all agree that this constitutional issue is important and recurring, the Court should grant the petition to resolve the conflicting decisions.

B. The Broader – and Also Recurring – Constitutional Questions Make this Case Even More Important.

The substantial importance of the narrow constitutional question presented is amplified by the constitutional controversies out of which that question arises: (1) whether or to what extent this Court's "continuity of transit" analysis applies to modern dormant Commerce Clause analysis after *Complete Auto*; and (2) whether the "physical-presence" requirement, which the Court reaffirmed in *Quill* as to *sales* and *use* taxation, likewise applies to ad valorem *property* taxation. The Court's answers to those questions will affect a far broader range of goods than natural gas.

1. The "Continuity of Transit" Issue is Important and Recurring.

As the Solicitor General explained in *Missouri Gas*, there are "two different lines of dormant Commerce Clause precedents." Br. for U.S. (No. 08-1458), at 9. "In its earlier cases, dating back to the late nineteenth century, this Court applied a 'continuity of transit' analysis to determine whether goods being transported through a State could be subjected to state property taxes." *Id.* "Under that approach, the critical question was whether the interstate transit of

goods had been sufficiently interrupted for purposes other than merely facilitating the transit; if so, the goods were deemed locally taxable." *Id.*, at 9-10.

"In *Complete Auto* this Court announced a new general framework for resolving dormant Commerce Clause challenges to state taxes." *Id.*, at 10. "The Court held that a state tax will be sustained against a dormant Commerce Clause challenge if it [satisfies the Court's four-pronged test]." *Id.* "The Court also overruled its prior holdings that any tax on the 'privilege of doing [interstate] business' was unconstitutional per se." *Id.* (citing *Complete Auto*, 430 U.S., at 288-89). "As compared to the Court's prior 'continuity of transit' decisions, the *Complete Auto* framework requires a more comprehensive inquiry, consistent with the Court's rejection of the per se rule against state taxation of interstate commerce." *Id.*

The Texas court of appeals in this case focused heavily on this Court's "continuity of transit" line of authorities, citing a whole string of pre-*Complete Auto* decisions.[5] Based on those authorities, the court concluded that "[t]he crucial question in determining whether the state may exert its taxing power is

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[5] *See* App., *infra*, 11-14, 17 (citing *Coe v. Errol*, 116 U.S. 517, 527 (1886); *Hughes Bros. Timber Co. v. Minnesota*, 272 U.S. 469, 476 (1926); *Indep. Warehouses v. Scheele*, 331 U.S. 70, 73 (1947); *Carson Petroleum Co. v. Vial*, 279 U.S. 95, 101 (1929); *Blasius*, 290 U.S., at 9-10; *Champlain Realty Co. v. Town of Brattleboro*, 260 U.S. 366, 377 (1922); and *Mich.-Wis. Pipe Line Co. v. Calvert*, 347 U.S. 157, 166-68 (1954)).

whether there is 'continuity of transit.'" App., *infra*, 13. The Texas court then concluded that "[t]he natural gas allocated to Peoples is in the stream of interstate commerce, and this storage does not remove it from interstate commerce." *Id.*, at 17.

Having made the threshold determination that the gas allocated to Peoples was in "continuity of transit," the court, in its ensuing *Complete Auto* analysis, attached little significance to the fact that large volumes of the gas were continuously present in Harrison County, Texas. The court also found it compelling that Pipeline, not Peoples, decided where the gas was to be stored. App., *infra*, 19-20. Under that analysis, the court held the connection between the State of Texas and Peoples' large inventories of storage gas in Texas to be "too tenuous to subject Peoples to ad valorem taxation in Texas." *Id.*, at 20.

In direct conflict with that approach, the Supreme Court of Oklahoma rejected the Texas court's reliance on the "traditional continuity of transit analysis" because it was "superseded by the Supreme Court's decision in *Complete Auto Transit v. Brady*." *Missouri Gas*, 234 P.3d, at 959 n.84. The Court also rejected as immaterial to the *Complete Auto* analysis the factor that the Texas court found to be compelling – that Pipeline, not Peoples, was "the decision maker with respect to the place of storage. . . ." *Id.*

As noted above, the Solicitor General observed that this Court has yet to decide whether or to what extent the "continuity of transit" analysis retains

vitality in Commerce Clause analysis. Br. for U.S. (No. 08-1458), at 10. The Supreme Court of Oklahoma noted the same dearth of authority: "While the [U.S. Supreme] Court has applied the [*Complete Auto*] test to many kinds of taxes, it has never addressed whether the [*Complete Auto*] test applies to an ad valorem tax on goods in the process of being transported in interstate commerce." *Missouri Gas*, 234 P.3d, at 953 (citing *Complete Auto*, 430 U.S. at 279).

A leading tax commentator has likewise noted this lack of clarity. Although "[s]ome of the results of the doctrinal changes" brought about by this Court in recent years "are clear," "the impact of the contemporary Commerce Clause philosophy on other cases decided in earlier eras, and the doctrine they spawned, is less clear." 1 J. Hellerstein & W. Hellerstein, State Taxation ¶ 4.13[1] (3d ed. 2010).

The continuing uncertainty about the role, if any, of "continuity of transit" implicates the full range of goods that taxpayers might argue are in the course of interstate transport. A recent example is a decision holding that oil in a tank farm is immune from state property taxation. *See Midland Cent. Appraisal Dist. v. BP Am. Production Co.*, 282 S.W.3d 215, 224 (Tex. App. – Eastland 2010, pet. denied). Relying on this Court's pre-*Complete Auto* jurisprudence, and citing the decision below, the *Midland Central* court held that because the oil was "in transit in the stream of interstate commerce," state property taxation of the oil was prohibited by the Commerce Clause. *Id.* A petition for a writ of certiorari is likewise being filed

in the *Midland Central* case today. The simultaneous pendency before this Court of these cases illustrates that not only is the "continuity of transit" issue recurring, but it implicates a far broader range of goods than natural gas. Industry, States, and local governments would all benefit from clarification.

2. The "Physical-Presence" Issue is Important and Recurring.

The Texas court concluded that the tax at issue violated the Commerce Clause because it did not satisfy the first prong of *Complete Auto* – "substantial nexus." App., *infra*, 21. Again, having concluded that the gas was in "continuity of transit" in interstate commerce, the court attached little significance to the large amounts of Peoples' gas that were continuously present in Harrison County, Texas. Rather than focus on the presence of the *gas* in storage in Harrison County – the object of the state ad valorem property tax – the court focused instead on the presence of the *taxpayer*: "Peoples maintains no office in Texas. Nor does it have any employees, representatives, or physical facilities in the State." *Id.*, at 19. Because the taxpayer was absent from the State, the Texas court found no substantial nexus. *Id.*, at 21.

In support of its *taxpayer*-focused (not *property*-focused) analysis, the Texas court invoked *Quill*'s "physical-presence" rule: "The Commerce Clause requirement of a substantial nexus with the taxing state is satisfied by the taxpayer's physical presence

in the state." App., *infra*, 19 (citing *Quill*, 504 U.S., at 312-14). *Quill* involved a sales and use tax – not a property tax. In *Quill*, this Court invoked *stare decisis* in declining to renounce the "physical-presence" rule in cases involving Commerce Clause challenges to sales and use taxation. 504 U.S., at 317-18. The Court thereby let stand a bright-line rule that the Court originally adopted a decade before *Complete Auto* in *Nat'l Bellas Hess, Inc. v. Dep't of Revenue of Ill.*, 386 U.S. 753, 758 (1967).

Again, the Supreme Court of Oklahoma was "unpersuaded by [the Texas] court's reasoning." *Missouri Gas*, 234 P.3d, at 959 n.84. The Oklahoma court rejected the notion that the taxpayer's *in personam* contacts with the State should control for an ad valorem tax on *property*. *Id.* Rather, the Oklahoma court concluded that the fundamental question should be whether the taxpayer *owns property* in the jurisdiction that seeks to impose the ad valorem tax: "While this case certainly presents some complexity, the fundamental question is simple: does the taxpayer own property located in the county seeking to impose the ad valorem tax?" *Id.* "Nothing in the Texas appellate court's decision persuades us that the answer to the correctly formulated question is anything other than a resounding yes." *Id.*

The relevance of the taxpayer's physical presence in the State outside the context of sales and use taxation needs to be clarified. *See Quill*, 504 U.S., at 312-14. One can envision an entire range of situations in which the taxpayer itself might not have an *in*

personam type of "physical presence" in the State, yet could nonetheless own real or personal property in the State that would otherwise be subject to ad valorem taxation. If (as the Texas court held but the Oklahoma court disagreed) such property is beyond the reach of state taxation simply because the taxpayer itself "maintains no office[,] employees, representatives, or physical facilities in the State" (App., *infra*, 19), the adverse impact on state taxing authorities could be incalculable.

The scope of *Quill*'s "physical-presence" requirement is a recurring issue on which state courts are divided. *See Lanco, Inc. v. Dir., Div. of Taxation*, 908 A.2d 176, 177 (N.J. 2006) ("Since the Court decided *Quill*, a split of authority has developed regarding whether the Supreme Court's ['physical-presence'] holding was limited to sales and use taxes. . . . We believe that the better interpretation of *Quill* is the one adopted by those states that limit the Supreme Court's holding to sales and use taxes."), *cert. denied*, 551 U.S. 1131 (2007). Another petition now pending before this Court raises this issue with regard to a state income tax. *See Asworth, LLC v. Dep't of Revenue, Finance, and Admin. Cabinet*, No. 10-662. The present case presents this recurring issue in a narrower, but no less important, context: whether the "physical-presence" rule precludes state taxation where the taxpayer has *property* in the State, and that property is itself the object of the ad valorem tax at issue.

C. This Case Warrants Immediate Review.

This case cleanly presents both the narrow constitutional issue and the two broader constitutional controversies out of which it arises. The competing views of the law have already been analyzed by the Solicitor General as well as the lower courts. Further delay would neither frame the constitutional issue more cleanly nor enhance presentation of the competing arguments. Rather, the delay would only result in continuing confusion, when all concerned desire certainty. This is why even industry opponents of the tax at issue agree with state taxing authorities that this is "a recurring issue that merits this Court's attention." AGA Amicus Brief (No. 08-1458), at 3.

II. The Decision Below is Erroneous.

Three errors in the court of appeals' analysis particularly deserve this Court's attention.

A. The Court of Appeals Erred in Using this Court's "Continuity of Transit" Analysis to Eclipse the *Complete Auto* Analysis.

The Texas court of appeals erroneously concluded that this Court's traditional "continuity of transit" analysis remains "crucial" to the Commerce Clause inquiry. App., *infra*, 13. As the Supreme Court of Oklahoma correctly concluded, that analysis has effectively been "superseded by the Supreme Court's

decision in *Complete Auto*." *Missouri Gas*, 234 P.3d, at 959 n.84.

Examples of this Court's cases employing the older "continuity of transit" analysis include *Blasius*, 290 U.S., at 9-12, and *Bacon v. Illinois*, 227 U.S. 504, 511-17 (1913). The Solicitor General explained the analysis employed in those cases: "Under that approach, the critical question was whether the interstate transit of goods had been sufficiently interrupted for purposes other than merely facilitating the transit; if so, the goods were deemed locally taxable." Br. for U.S. (No. 08-1458), at 9-10. Correspondingly, if the goods were determined to be "in transit in interstate commerce," they were deemed immune from state taxation. *See Blasius*, 290 U.S., at 9. Thus, under the traditional approach, "the 'crucial question' . . . is . . . 'continuity of transit.'" *Id.* (quoting *Carson Petroleum Co. v. Vial*, 279 U.S. 95, 101 (1929)). The question was "crucial" in that bygone era because it was determinative of the State's taxing power.

In contrast, after *Complete Auto*, deciding whether goods are *in* or *out* of the stream of interstate commerce – the objective of the "continuity of transit" test – is no longer determinative. In *Complete Auto*, this Court "rejected the notion that state taxes levied on interstate commerce are *per se* invalid." *Commonwealth Edison Co. v. Montana*, 453 U.S. 609, 615 (1981) (citing *Complete Auto*, 430 U.S., at 288-89). Correspondingly, it is no longer true that determining goods to be *out* of the stream of interstate commerce necessarily means that they are locally

taxable. Rather, this Court has "long since rejected any suggestion that a state tax or regulation affecting interstate commerce is immune from Commerce Clause scrutiny because it attaches only to a 'local' or intrastate activity." *Id.*

In short, although the "continuity of transit" analysis was once determinative of the Commerce Clause inquiry, it no longer is. What is determinative today is whether the state tax satisfies the *Complete Auto* four-pronged test. If it does, "no impermissible burden on interstate commerce will be found." *Japan Line, Ltd. v. Los Angeles County*, 441 U.S. 434, 444-45 (1979). Thus, *Complete Auto* has effectively displaced the "continuity of transit" analysis, and the court below erred in granting the latter preeminence.

B. The Court of Appeals Erred in Applying *Quill*'s "Physical-Presence" Rule to Ad Valorem Property Taxation.

Having concluded that Peoples' gas was in "continuity of transit" in interstate commerce, the court of appeals attached little significance to the massive presence of Peoples' storage gas in Harrison County, Texas. Instead, the court supported its conclusion that the Commerce Clause prohibits the state tax at issue by noting that the taxpayer, Peoples, has no office, employees, representatives, or physical facilities in the State. App., *infra*, 19.

Yet the absence of such *in personam* contacts with the State is irrelevant when the tax at issue is

one on *property*. For a property tax, the constant physical presence of an inventory of the property in the State should be sufficient to satisfy the requisite link between the State and the property sought to be taxed. *See Allied-Signal, Inc. v. Dir., Div. of Taxation*, 504 U.S. 768, 777 (1992) (reciting as a "fundamental requirement of both the Due Process and Commerce Clauses that there be 'some definite link, some minimum connection, between a *state* and the . . . *property* . . . it seeks to tax'") (emphasis added) (quoting *Miller Bros. v. Maryland*, 347 U.S. 340, 344-45 (1954)). The requisite connection between the *State* and the *property* in this case is substantial.

In holding otherwise, the Texas court of appeals erroneously invoked this Court's decision in *Quill*. App., *infra*, 19 (citing *Quill*, 504 U.S., at 312-14). In *Quill*, the Court declined to overrule the requirement that the taxpayer be physically present in the State to justify imposing a *sales* or *use* tax.

Quill is explicitly narrow, and should be confined to sales and use taxes. *Quill* makes clear that the "physical-presence requirement" originally adopted in *Bellas Hess* was "established for sales and use taxes," and that "we have not, in our review of other types of taxes, articulated the same physical-presence requirement. . . ." 504 U.S., at 314. Alternatively, if this Court concludes that the "physical-presence" rule does apply outside the context of sales and use taxation, the Court should hold that the physical presence of the taxpayer's property in the State suffices to satisfy the rule, at least if that property is the object

of the ad valorem tax at issue. In either event, the Court should hold that the "physical-presence" requirement does not prohibit the ad valorem tax in this case.

C. The Court of Appeals Erroneously Held that the State Tax at Issue Fails the *Complete Auto* Test.

The court of appeals held that the state tax at issue fails the first and fourth prongs of the *Complete Auto* test. App., *infra*, 22. The court was wrong; the tax satisfies both of those prongs.[6]

1. The Tax is on Property that Has a "Substantial Nexus" with Texas.

The first prong of *Complete Auto* requires that the tax be "applied to an activity with a substantial nexus with the taxing State." 430 U.S., at 279. This Court has stated that it is a requirement of both the Due Process Clause and the Commerce Clause that there be some definite link, some minimum connection between a *state* and the *property* it seeks to tax. *Allied-Signal*, 504 U.S., at 777. *Property* – a large inventory of natural gas owned by Peoples and held in underground storage in Harrison County, Texas –

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[6] The tax satisfies the second and third prongs as well. But because the court of appeals did not address those two prongs in its opinion, the Appraisal District does not address them in this petition.

is what the Appraisal District seeks to tax here. Although volumes of Peoples' gas may come and volumes of gas may go, on any given day Peoples has in storage in Texas what can only be described as a massive inventory of natural gas. There is "substantial nexus" between that storage gas and the State of Texas, which suffices for the ad valorem tax at issue to survive constitutional scrutiny.

Professor Hellerstein agrees, concluding with specific regard to this case: "The physical presence of a 'significant volume' of the owner's property appears to be more than sufficient to constitute 'substantial nexus.'" Hellerstein & Hellerstein, *supra*, ¶ 4.13[3][a]. He found the court of appeals' holding to the contrary to be "highly questionable, if not plain error." *Id.*

The Solicitor General similarly concluded that "the nexus between Oklahoma and the 'large volumes of gas' stored there 'for a substantial part of the year' is sufficient to satisfy prong one of the *Complete Auto* test." Br. for U.S. (No. 08-1458), at 21. Exactly the same thing can be said of the large volumes of gas stored in Texas.

A property's mere physical presence in the State may not always suffice to establish "substantial nexus." The Solicitor General provided an example of an exception in *Missouri Gas*: "[T]he transportation of natural gas could be significantly burdened if multiple States attempted to tax the same volume of gas based solely on its movement through an interstate pipeline." Br. for U.S. (No. 08-1458), at 19. In light of this concern, the Supreme Court of Oklahoma limited

its holding to *storage* gas: "[C]oncluding that the natural gas at issue bore a constitutionally sufficient nexus to the taxing State, the Oklahoma Supreme Court carefully limited its holding to *stored* natural gas." *Id.*, at 19 n.6 (emphasis in original) (quoting *Missouri Gas*, 234 P.3d, at 954 (concluding that "[petitioner's] storage gas cannot be characterized as goods that are merely passing through the state")). A similarly limited holding in this case would not open the door to State taxation of commodities in pipelines.

2. The Tax is "Fairly Related to the Services Provided by the State."

The fourth prong merely requires that the tax be "fairly related to the services provided by the State." *Complete Auto*, 430 U.S., at 279. "The simple but controlling question is whether the state has given anything for which it can ask return." *Commonwealth Edison*, 453 U.S., at 625 (internal quotation marks omitted).

Consistent with these authorities, the Oklahoma Supreme Court correctly addressed the fourth prong in a manner applicable here:

> The tax in this case operates on the presence of personal property in Woods County. It is taxed to the same extent as all other personal property in the county. [Taxpayer] MGE is therefore being asked to shoulder no more than its fair share for the support of government-provided services and the receipt of "the advantages of a civilized society."

Missouri Gas, 234 P.3d, at 959 (quoting *Exxon Corp. v. Wisconsin Dep't of Revenue,* 447 U.S. 207, 228 (1980), quoting *Japan Line*, 441 U.S., at 445).

In contrast, the Texas court of appeals incorrectly focused on Pipeline's facility and cushion gas – not Peoples' working gas:

> While we do not doubt the value of [the] services [provided within the county], we note, again, that services such as law enforcement and the fire department would serve the North Lansing facility itself, and the facility undoubtedly belongs to Pipeline, which does pay ad valorem taxes on both the "cushion" gas it maintains in the facility and the physical plant of the facility itself.

App., *infra*, 21-22.

That Pipeline pays ad valorem taxes on its "cushion" gas and "the physical plant of the facility itself" in no way suggests that Peoples' *working* gas should be constitutionally excused from taxation. Peoples benefits from the storage of its working gas in Harrison County, and it should be no less responsible for ad valorem taxation of its working gas than Pipeline is for taxation of its cushion gas. Because Peoples substantially benefits from the storage of its gas, it "may be required to contribute to the cost of providing *all* governmental services, including those services from which it arguably receives no direct 'benefit.'" *Commonwealth Edison*, 453 U.S., at 628 n.16 (emphasis in original).

That Pipeline's "physical plant of the facility itself" is taxed (App., *infra*, 22) is immaterial. The need for fire protection, for example, arises not from the physical plant itself so much as it does from the billions of cubic feet of natural gas stored within the facility.

As with the first prong, Professor Hellerstein concluded that the court of appeals' decision regarding the fourth prong is "highly questionable, if not plain error." Hellerstein & Hellerstein, *supra*, ¶ 4.13[3][a]. He sees "no basis for the conclusion that the taxpayer's gas does not receive 'police and fire protection . . . and the advantages of a civilized society.'" *Id.* This Court should reach the same conclusion.

CONCLUSION

The Court should grant the petition for writ of certiorari.

Respectfully submitted,

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[SEAL]

In The
Court of Appeals
Sixth Appellate District of Texas at Texarkana

No. 06-07-00103-CV

THE PEOPLES GAS, LIGHT,
AND COKE COMPANY, Appellant

V.

HARRISON CENTRAL
APPRAISAL DISTRICT, Appellee

On Appeal from the 71st Judicial District Court
Harrison County, Texas
Trial Court No. 05-0381

Before Morriss, C.J., Carter and Moseley, JJ.
Opinion by Chief Justice Morriss

OPINION

The large amount of natural gas ordinarily stored under Harrison County has great value. The Harrison Central Appraisal District (the District) has acted to assess a large ad valorem tax bill against a portion of that gas—gas allocable to the account of Peoples Gas, Light, and Coke Company (Peoples). From a judgment favoring the District, Peoples appeals.

The gas in question is stored in a large, depleted natural gas field now used as a natural gas storage facility—the North Lansing facility—part of the interstate pipeline system operated by Natural Gas Pipeline Company of America (Pipeline). Peoples is a distribution company that purchases natural gas from suppliers and delivers it to users in Chicago, Illinois. Pipeline, not a party to this matter, operates the interstate pipeline system pursuant to regulations promulgated by the Federal Energy Regulatory Commission (the Commission). Peoples buys natural gas already on the interstate pipeline system owned and operated by Pipeline. Pipeline representatives testifying at trial emphasize that there are many storage facilities associated with its pipeline and that the pipeline is operated "in the aggregate." In other words, Pipeline's storing and transporting gas does not use any particular storage field exclusively.

Pipeline pays ad valorem taxes on what is called "cushion gas" in North Lansing, the significant volume of natural gas that remains in the storage facility and provides the necessary pressure and balance to facilitate the safe, efficient operation of the pipeline. Beginning in 1999, the District allocated to Peoples a portion of the "working" natural gas balance—the volume of gas (above the "cushion") that is transported and delivered to pipeline customers—and assessed taxes on the value of that portion of the natural gas stored at North Lansing. Peoples successfully challenged the assessment and, on advice of its appraisal

consultant firm, the District removed Peoples from the tax rolls. The same thing happened in 2000.

For tax years 2003-2005, the District again attempted to assess taxes against Peoples on a portion of the gas stored at North Lansing. This time, on advice from a new consultant firm, the District refused to remove Peoples from the tax rolls. Instead, the District assessed Peoples' portion of the gas at North Lansing, for those years, at values exceeding nine million, forty million, and forty-three million dollars, respectively. Those tax years and tax levies are at issue in this case.

The gas volume figures allocable to Peoples are based on Pipeline's records.[1] Pipeline compares the total contractual balance for all the NSS[2] shippers that have contracts on Pipeline's Gulf Coast Leg to the "working" natural gas balance at North Lansing at the end of the year. This yields a percentage that is multiplied by each shipper's NSS contractual balance on the Gulf Coast Leg of the pipeline at the end of the

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[1]Pipeline's representative explained that its allocation methods were not for the purpose of determining ownership. It merely did what it was asked to do for the courts to decide the issue of ownership.

[2]Pursuant to Commission tariffs, Pipeline offers several types of contracts to shippers on its pipeline system. Most common are the "NSS" and "DSS" contracts. NSS storage requires a customer such as Peoples to request or nominate a withdrawal to get delivery on a date certain. DSS storage service, on the other hand, allows for no-notice delivery.

year to arrive at the allocation it attributes to a customer.

The trial court ruled that the District has the authority to assess the ad valorem taxes for the years in question on the gas it allocated to Peoples. We review de novo the trial court's conclusions of law determining each question of law independently. *Quick v. City of Austin,* 7 S.W.3d 109, 116 (Tex. 1999). We review the trial court's findings of fact for legal and factual sufficiency, as we do with jury findings. *See Ashcroft v. Lookadoo,* 952 S.W.2d 907, 910 (Tex. App.—Dallas 1997, pet. denied).

Our analysis leads us, through the following logical steps, to conclude that taxing this gas infringes the Commerce Clause:

(1) Peoples owns this gas for ad valorem tax purposes.

(2) The Commerce Clause shields this gas from ad valorem taxation.

  (A) This gas is in interstate commerce.

  (B) This storage does not remove this gas from interstate commerce.

  (C) The District cannot tax this gas.

For these reasons, we reverse the judgment of the trial court and render judgment that assessing these ad valorem property taxes for these years was improper.

(1) Peoples Owns this Gas for Ad Valorem Tax Purposes

The District and Peoples agree that, under the Commission's regulations, Pipeline does not own the gas in its pipeline system. Peoples contends that it does not own, for ad valorem tax purposes, any amount of the massive volume of natural gas lying beneath Harrison County; the District responds that someone must own the gas, and, since Pipeline certainly does not, Peoples *must* be the taxable owner of the portion of the gas allocable to its account.

"Property taxes are the personal obligation of the person who owns or acquires the property on January 1 of the year for which the tax is imposed." TEX. TAX CODE ANN. § 32.07(a) (Vernon 2008). The Texas Tax Code does not define "own" or "owner" for purposes of assessing ad valorem taxes. Texas courts have generally defined taxable "owner" as the individual or entity holding legal title to the property or holding an equitable right to obtain legal title. *See Childress County v. State,* 127 Tex. 343, 92 S.W.2d 1011, 1015 (1936); *Travis Cent. Appraisal Dist. v. Signature Flight Support Corp.,* 140 S.W.3d 833, 840 (Tex. App.—Austin 2004, no pet.); *Comerica Acceptance Corp. v. Dallas Cent. Appraisal Dist.,* 52 S.W.3d 495, 497 (Tex. App.—Dallas 2001, pet. denied). If an individual or entity does not hold perfect legal title, however, that individual or entity may still be considered the taxable owner of property "if he is the record owner, or is vested with the apparent legal title, or is in possession thereof, coupled with such claims and evidences

of ownership as will justify the assumption that he is the owner thereof." *Childress County,* 92 S.W.2d at 1015; *Signature Flight Support Corp.,* 140 S.W.3d at 840. The term "owner" has no fixed legal meaning:

> The meaning of the term owner is not the same under all circumstances. It is not a technical term or word at all, but one of wide application in various connections. In all instances its meaning must be ascertained from the context and subject matter.

Realty Trust Co. v. Craddock, 131 Tex. 88, 112 S.W.2d 440, 443 (1938); *see Signature Flight Support Corp.,* 140 S.W.3d at 839. That said, we examine the "context and subject matter" here to determine whether Peoples owns the gas in question.

We begin with a short explanation of the highly regulated natural gas transportation and storage system and the dealings between Pipeline and its customers, including Peoples. The Commission restructured the natural gas transport and storage industry in 1992. This restructuring created a system of commercial rights for the pipeline customer that was separate from the physical operation of the pipeline system. Buyers and sellers conduct transactions at commercial points—"paper points" or imaginary points—along the pipeline at which a purchase may be completed, points that do not necessarily reflect the physical location of the gas purchased. Pursuant to this restructuring and to facilitate purchase transactions, Pipeline established geographical zones, such as the South Texas zone, the "TEX-OK"

zone, and the Iowa-Illinois zone, which help identify the distance the gas is transported from the point at which it was injected into the pipeline system.

Applying the *Comerica/Travis County* test, we conclude Peoples is the owner for ad valorem taxation purposes. As the parties agree, Pipeline has complete control of the physical operation of the pipeline system. Pipeline decides where and when the natural gas is stored. There is no physical connection between a Pipeline customer's storage account balance and physical volumes at any particular storage facility. The District acknowledges that Pipeline's accounting methods are completely divorced from the physical reality of the natural gas location. Pipeline's customers purchase volumes of natural gas at what the parties refer to as a "paper" pooling point after which time, Peoples emphasizes, the purchaser retains no control to direct the physical movement of the natural gas purchased. Peoples also emphasizes that Pipeline's storage fields are operated on an aggregated basis. That is, none of its services are specifically linked to any particular storage field.

Relevant documents show that Peoples purchased natural gas and paid for its transportation to the Iowa-Illinois zone. Of course, the fungible and ethereal nature of natural gas makes it impossible to ascertain the physical location of a given allocated portion of natural gas at any moment. Peoples contends that this documentary evidence in the form of Commission-approved agreements between Peoples and Pipeline suggests that Peoples' allocation of

natural gas is "contractually" located in the Iowa-Illinois zone. Obviously, Pipeline cannot identify particular volumes of gas as belonging to a particular customer when physically transporting or storing natural gas.

Consistent with Commission regulations, Pipeline is in full custody, control, and possession of the natural gas within the pipeline system. Only Pipeline can direct the physical movement of the gas once it is placed in the pipeline; and, even after a purchase of gas at a paper pooling point, the purchaser obtains no control over the physical movement of the volume of natural gas purchased. Peoples has no legal right to the natural gas located at North Lansing; it cannot specifically request gas from that facility and could not merely back a truck up to the facility and remove any amount of natural gas. Nor is there any indication that it could do any such thing in Illinois. Peoples emphasizes that it owns merely contractual rights to physically receive natural gas in Chicago and that its purchases from Pipeline call for contractual storage in the Iowa-Illinois zone.

Nonetheless, by regulation, ownership rights could not be transferred to Pipeline. That said, according to the District, legal title must lie with Peoples. No doubt gas is stored beneath Harrison County; there must be an owner of that gas for tax purposes. Considering the nature of the product at issue here, the nature of the pipeline in which customers' fungible goods must be commingled, and the highly regulated industry in which Pipeline and

Peoples conduct their business and which prohibits Pipeline from having ownership rights in the gas but requires that it maintain physical control of the natural gas, we conclude the trial court correctly decided that, for tax purposes, Peoples owns an allocation of the natural gas stored in Harrison County.[3]

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[3]Last year, the Kansas Supreme Court decided a case similar to the instant case. *See In the Matter of the Appeal of the Director of Prop. Valuation,* 284 Kan. 592, 161 P.3d 755 (2007). In that case, several non-Kansas entities (municipal utilities, natural gas marketing company, and public utilities) had contracted for gas storage or deferred delivery with an interstate pipeline that maintained storage facilities in Kansas. *Id.* The parties stipulated that none of the entities had facilities within Kansas or sold, traded, or delivered natural gas anywhere in Kansas. *Id.* at 594. In Kansas, a public utility's property is not exempt from ad valorem taxes. The taxing entity argued that non-Kansas companies were public utilities within the following definition: "that own, control, and hold for resale stored natural gas in an underground formation in this state." *Id.* at 597. Based on the legal and contractual relationship between the pipeline and its customers established by Commission-approved tariffs, the Kansas Supreme Court concluded the entities were not public utilities because they did not "control" and "hold for resale" the stored natural gas. *Id.* at 606. With that, the non-Kansas companies' allocations were exempt from ad valorem taxes. It did, however, touch on the ownership aspect of the "public utility" definition:

> There is no serious dispute that the Taxpayers own (or at least hold contractual rights to) storage balances of natural gas contained in underground formations in the state. Nevertheless, whether the Taxpayers actually control and hold the natural gas is doubtful. It is undisputed that tariffs issued by the . . . Commission . . . establish that control and possession

(Continued on following page)

(2) The Commerce Clause Shields this Gas from Ad Valorem Taxation

Peoples argues that, even if it could be said that it is the taxable owner in this matter, the Commerce Clause shields it from the District's assessment since the natural gas is in interstate commerce and since the tax cannot pass the test that would permit the District to assess such a tax on this property. We agree.

The Commerce Clause grants Congress the power to regulate interstate commerce. U.S. CONST. art. I, § 8, cl. 3. Congress protects interstate business activity by restricting state regulation of interstate commerce.[4] *See Marathon Ashland Petroleum, L.L.C. v. Galveston Cent. Appraisal Dist.*, 236 S.W.3d 335, 337-38 (Tex. App.—Houston [1st Dist.] 2007, no pet.).

> of natural gas delivered to interstate pipelines for transportation and storage is vested in the pipelines until the gas is redelivered to their customers. It is also undisputed that the interstate pipelines cannot track and account for discrete packages or molecules of natural gas delivered for storage. As the Supreme Court said in *Central Illinois*, under federal regulations the pipeline customers have "little or no control over where the severed natural gas is stored or for how long."

Id. at 603. Our conclusion on the ownership issue is consistent with the Kansas Supreme Court's conclusion.

[4]Congress has granted the Commission exclusive jurisdiction to regulate the natural gas industry through the Natural Gas Act (NGA). *Schneidewind v. ANR Pipeline Co.*, 485 U.S. 293 (1988).

(a) This Gas Is in Interstate Commerce

Traditionally, the United States Supreme Court has identified three ways in which goods can enter the stream of interstate commerce: (1) the goods have been shipped, (2) the goods have been placed with a common carrier, or (3) the goods have started a continuous route or journey into interstate commerce. *See Coe v. Errol,* 116 U.S. 517, 527 (1886); *Marathon Ashland Petroleum, L.L.C.,* 236 S.W.3d at 338. The goods become a part of interstate commerce when their movement demonstrates that the goods have started and are bound for another state. *See Hughes Bros. Timber Co. v. Minnesota,* 272 U.S. 469, 476 (1926). Goods are not a part of interstate commerce when the record shows only preparation or intent to send those goods out of state. *See id.*; *Marathon Ashland Petroleum, L.L.C.,* 236 S.W.3d at 340-41.

Here, it is apparent that the natural gas has been placed with a common carrier, Pipeline. Unlike the taxpayer in *Marathon Ashland Petroleum, L.L.C.,* Peoples does not maintain any control over the physical movement of the gas. Moreover, that common carrier is an interstate pipeline specifically governed by the Commission. There is little dispute that the natural gas in the *pipeline* is in interstate commerce. A critical question is whether the gas in North Lansing storage is similarly in interstate commerce.

(b) This Storage Does Not Remove this Gas from Interstate Commerce

The District takes the position that, although an extremely small portion of the natural gas (that portion actually moving in the pipeline) is actually in interstate commerce, the rest of the natural gas is stored and therefore subject to local taxation wherever it is located. More specifically, the District argues that the fact that the portion of natural gas allocated to Peoples here is not actually moving in the pipeline and is, rather, stored beneath Harrison County takes the gas outside interstate commerce, leaving it subject to taxation as a part of the mass of property within the State of Texas. *See Coe,* 116 U.S at 527; *Marathon Ashland Petroleum, L.L.C.,* 236 S.W.3d at 338.

We conclude this contention fails in the face of two areas of the law: authorities determining the effect of transportation stoppage on whether a product is in interstate commerce and authorities more specifically addressing storage of natural gas.

First, we look to the line of cases examining generally the circumstances surrounding the stoppage of products that have been injected into the stream of interstate commerce and determining whether a stoppage in a jurisdiction would subject the goods to local taxation. *See Indep. Warehouses, Inc. v. Scheele,* 331 U.S. 70, 73 (1947); *see also Virginia Indonesia Co.*

v. Harris County Appraisal Dist., 910 S.W.2d 905, 912-13 (Tex. 1995).[5] When there is a break in the interstate transit, the property may come to rest within a state and become subject to the power of the state to impose a nondiscriminatory property tax. *Indep. Warehouses, Inc.*, 331 at 72-73. The crucial question in determining whether the state may exert its taxing power is whether there is "continuity of transit." *Id.* at 73 (citing *Carson Petroleum Co. v. Vial*, 279 U.S. 95, 101 (1929)). The United States Supreme Court explained the concept:

> If the interstate movement has begun, it may be regarded as continuing, so as to maintain the immunity of the property from state taxation, despite temporary interruptions due to the necessities of the journey or for the purpose of safety and convenience in the course of the movement. . . . Formalities, such as the forms of billing, and mere changes in the method of transportation do not affect the continuity of the transit. The question is always one of substance, and in each case it is necessary to consider the particular occasion or purpose of the interruption during which the tax is sought to be levied. . . .

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[5]In *Virginia Indonesia Company*, the Texas Supreme Court determined whether the Import-Export Clause would permit imposition of an ad valorem tax. Similar considerations are involved when determining the "continuity of transit" for purposes of the Commerce Clause. *See* 910 S.W.2d at 912.

Id. (quoting *Minnesota v. Blasius,* 290 U.S. 1, 9-10 (1933)). We must look at the facts of each case and will consider the owner's intention, the owner's ability to change destination, the agency or method of transportation, the actual continuity of the journey, and the purpose of the interruption. *See Champlain Realty Co. v. Town of Battleboro,* 260 U.S. 366, 377 (1922).

The character of the shipment in such a case depends on the circumstances, including what the owner has done to prepare for the journey and to carry it out. *Virginia Indonesia Co.,* 910 S.W.2d at 912-13. For instance, when the stoppage of property in interstate commerce is necessary for the safety and convenience of the goods, we do not consider the continuity of transit broken. *Indep. Warehouses, Inc.,* 331 U.S. at 73. On the other hand, if the stoppage is attributable to the business purpose of the owner, then we deem the continuity of transit terminated and the goods are subject to tax in the jurisdiction of the stoppage. *Virginia Indonesia Co.,* 910 S.W.2d at 912. Put another way,

> [w]here property has come to rest within a State, being held there at the pleasure of the owner, for disposal or use, so that he may dispose of it either within the State, or for shipment elsewhere, as his interest dictates, it is deemed to be a part of the general mass of property within the State and is thus subject to its taxing power.

Indep. Warehouses, Inc., 331 U.S. at 73.

In the instant case, the record shows and the law requires that Peoples has no control over the physical operations of the pipeline. Control lies solely with Pipeline. Since Peoples has no control over where that natural gas is stored and how much is stored at any given location, we cannot say that Peoples made the decision to store gas at North Lansing in order to serve its business purpose. Simply put, it made no decision at all regarding the physical location of the stored natural gas.

The District contends Peoples benefits from the storage at North Lansing since it can buy gas at a cheaper rate in the summer months and store it for later use in the winter months when the demand in the Chicago area increases dramatically. It may well be the case that the advent of a pipeline system that will allow for storage of a significant amount of natural gas is beneficial to local distributing companies generally. Indeed, such a system would seem to be beneficial to all. Such a benefit, however, does not alter the fact that Peoples, while benefitting from a storage system generally, makes no decision to store the natural gas at North Lansing specifically. The record shows that the contracts between Peoples and Pipeline do not specify that the gas would be located in Texas. In fact, those agreements provide for "contractual" storage in Iowa and Illinois. The truth is, Pipeline operates its system without regard to the physical reality of identifying a specific storage facility at which any customer's volume of natural gas will be physically stored. Rather, Pipeline operates

the pipeline on an "aggregate" basis in which all the storage facilities serve the pipeline as needed to operate efficiently and effectively. With these facts in mind, we conclude that the stoppage of natural gas in North Lansing does not serve the business purpose of Peoples. To the contrary, Peoples has no control over where the natural gas is stored, and we cannot say that the stoppage in Harrison County serves a business purpose as contemplated by the cases dealing with the continuity of transit of goods in interstate commerce.

Second, we examine law specifically concerning the storage of natural gas. Commission regulations provide some guidance as to whether storage would take the natural gas out of the stream of interstate commerce: "Transportation includes storage, exchange, backhaul, displacement, or other methods of transportation." 18 C.F.R. § 284.1(a). By regulation, then, at least some storage is considered a part of the transportation process. Therefore, storage can be a part of *interstate* transportation. Storage in North Lansing, then, as a matter of regulatory definition, would not necessarily take the natural gas out of the stream of interstate commerce.

Indeed, the United States Supreme Court has spoken on this issue:

> Petitioners argued below that Storage was not a natural gas company within the meaning of the NGA, contending that the storage of gas constitutes neither the transportation nor the sale of gas in interstate commerce.

> Both courts below rejected this argument . . . reasoning that "transportation" includes storage. "Underground gas storage facilities are a necessary and integral part of the operation of piping gas from the area of production to the area of consumption."

Schneidewind, 485 U.S. at 295 n.1 (quoting *Columbia Gas Transmission Corp. v. Exclusive Gas Storage Easement,* 776 F.2d 125, 129 (6th Cir. 1985)); *see also Michigan-Wisconsin Pipe Line Co. v. Calvert,* 347 U.S. 157, 166-68 (1954) (evaluating Texas tax on "gathering" gas in context of interstate pipeline, characterizing situation and "so closely related to interstate transportation as to be practically a part of it," and concluding that the tax in that situation violated Commerce Clause). This storage of this natural gas in North Lansing does not take the gas out of interstate commerce. To conclude otherwise would be to segregate, from the pipeline itself, a function deemed "necessary and integral" to the pipeline. We will not do so and, instead, conclude that this storage does not take this natural gas out of the stream of interstate commerce it entered by injection into an interstate pipeline. The natural gas allocated to Peoples is in the stream of interstate commerce, and this storage does not remove it from interstate commerce.

(c) The District Cannot Tax this Gas

It remains possible that the District could still have the authority to tax the portion of natural gas allocated to Peoples, despite the fact that the natural

gas has been injected into and remains within the stream of interstate commerce. A state tax does not violate the Commerce Clause if it (1) is applied to an activity with a substantial nexus with the taxing state, (2) is fairly apportioned, (3) does not discriminate against interstate commerce, and (4) is fairly related to the services provided by the state. *See Vinmar v. Harris County Appraisal Dist.*, 947 S.W.2d 554, 555 (Tex. 1997) (citing *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 279 (1977)); *Diamond Shamrock Ref. and Mktg. Co. v. Nueces County Appraisal. Dist.*, 876 S.W.2d 298 (Tex. 1994); *Rylander v. 3 Beall Bros. 3, Inc.*, 2 S.W.3d 562, 570 (Tex. App.—Austin 1999, pet. denied). If a tax does not satisfy this test, called the *Complete Auto* test, the Commerce Clause prohibits the tax. *See Harris County Appraisal Dist. v. Transamerica Container Leasing, Inc.*, 920 S.W.2d 678, 682 (Tex. App.—Houston [1st Dist.] 1995, writ denied). The second and third parts of the *Complete Auto* analysis, which require fair apportionment and nondiscrimination, prohibit taxes that pass an unfair share of the tax burden onto interstate commerce. *Quill Corp. v. N.D.*, 504 U.S. 298, 313 (1992). The first and fourth prongs, which require a substantial nexus and a relationship between the tax and state-provided services, limit the reach of state taxing authority so as to ensure that state taxation does not unduly burden interstate commerce. *Id.*

The Commerce Clause requires "some definite link, some minimum connection,[6] between a state and the person, property, or transaction it seeks to tax." *Allied-Signal, Inc. v. Director, Division of Tax,* 504 U.S. 768, 777 (1992) (quoting *Miller Bros. v. Maryland,* 347 U.S. 340, 344-45 (1954)); *3 Beall Bros. 3, Inc.,* 2 S.W.3d at 570. The Commerce Clause requirement of a substantial nexus with the taxing state is satisfied by the taxpayer's physical presence in the state. *3 Beall Bros. 3, Inc.,* 2 S.W.3d at 570; *Lawrence Indus., Inc. v. Sharp,* 890 S.W.2d 886, 892-93 (Tex. App.—Austin 1994, writ denied); *see also Quill Corp.,* 504 U.S. at 312-14.

The record demonstrates that Peoples maintains no office in Texas. Nor does it have any employees, representatives, or physical facilities in the State. The physical facilities in Harrison County belong to Pipeline, as does the decision to use the North Lansing facility. Further, there is no evidence that any of the natural gas Peoples has purchased is delivered to any customer in Texas.

If we were to look strictly at the generic act of storing gas in a reservoir in Harrison County, it

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[6]The "substantial nexus" requirement is not, like due process' "minimum contacts" requirement, a proxy for notice, but rather a means for limiting state burdens on interstate commerce. *Quill Corp.,* 504 U.S. at 313. Accordingly, an entity may have the "minimum contacts" with a taxing state as required by the Due Process Clause, and yet lack the "substantial nexus" with that state as required by the Commerce Clause. *Id.*

might appear that such an activity would have a substantial nexus with the State. We note again that, as required by the Commission regulations, Pipeline—not Peoples—directs that activity, and we are to consider not whether Pipeline's activities have a substantial nexus with the State, but whether Peoples' activities do. Peoples engages in the purchase and delivery of natural gas to its customers in Chicago. Its only connection in this respect to Texas is through the structure and location of Pipeline's pipeline and Pipeline's decision to store a significant amount of natural gas in North Lansing. Such a connection is too tenuous to subject Peoples to ad valorem taxation in Texas.[7]

The District contends the nexus lies between the natural gas and the State. The natural gas, it argues, comes from Texas and is, thus, substantially connected to the State such that the State should be allowed to tax it. The record suggests that much of the gas is Texas-produced. Nevertheless, we do not have specific

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[7]We also note our sister court's opinion in *Rylander v. Bandag Licensing Corp.*, 18 S.W.3d 296 (Tex. App.—Austin 2000, pet. denied). In *Bandag Licensing Corp.*, the Austin court suggests that "when the corporation conducts its activity solely through interstate commerce and lacks any physical presence in the state, no sufficient nexus exists to permit the state to assess tax." *Id.* at 300. That connection, along with the facts that the corporation's only activity was the "passive possession of a license to do business in Texas" and that the corporation had no physical presence in Texas, led the court to conclude that the Commerce Clause prohibited the imposition of a state tax in that situation.

volumes of that production, nor could we ever know the location from which Peoples' allocation originated.

We conclude that, despite the fact that Peoples owns some of the natural gas on the system and thus under Harrison County, the storage of natural gas at the North Lansing field is an insufficient nexus when we consider the particular, unique circumstances at hand and the complex relationships among the parties involved. We find insufficient nexus between Texas and the entity, property, or transaction to be taxed. That said, the District's tax fails to satisfy the first prong of the *Complete Auto* test and, therefore, violates the Commerce Clause.

Moving to other parts of the test, we look at the relation between Peoples and services provided in Harrison County. Under the Commerce Clause, the measure of the tax must be reasonably related to the extent of the taxpayer's presence or activities within the taxing state and to the taxpayer's consequent enjoyment of the opportunities which the state has afforded. *3 Beall Bros. 3, Inc.,* 2 S.W.3d at 571. Even though fire and police services may not be invoked, protection conferred by these "along with the usual and usually forgotten advantages conferred by the state's maintenance of a civilized society are justifications enough for the imposition of a tax." *See Transamerica Container,* 920 S.W.2d at 683. The District presented substantial evidence of services provided within the county. While we do not doubt the value of those services, we note, again, that services such as law enforcement and the fire department

would serve the North Lansing facility itself, and the facility undoubtedly belongs to Pipeline, which does pay ad valorem taxes on both the "cushion" gas it maintains in the facility and the physical plant of the facility itself.

Having found that the District's tax on Peoples' gas fails to meet, at least, the first and fourth prongs of the *Complete Auto* test, we conclude that assessment of ad valorem taxes, on these facts, runs afoul of the Commerce Clause.

We reverse the trial court's judgment and render judgment that assessing these ad valorem property taxes for these years is improper.

Josh R. Morriss, III
Chief Justice

Date Submitted: June 18, 2008
Date Decided: September 24, 2008

[SEAL]

Court of Appeals
Sixth Appellate District of Texas

JUDGMENT

The Peoples Gas, Light and Coke Company, Appellant		Appeal from the 71st Judicial District Court of Harrison County, Texas (Tr. Ct. No. 05-0381). Opinion delivered by Chief Justice Morriss, Justice Carter and Justice Moseley participating.
No. 06-07-00103-CV	V.	
Harrison Central Appraisal District, Appellee		

BE IT REMEMBERED, that in accordance with the Court's opinion of this date, the Court finds that there was error in the judgment below. Therefore, it is **ORDERED** that the judgment of the court below is **REVERSED** and judgment is **RENDERED** that the natural gas in the North Lansing facility, allocable to Peoples Gas, Light, and Coke Company is not subject to the ad valorem taxes assessed by Harrison Central Appraisal District for tax years 2003-2005.

It is further **ORDERED** that the appellee, Harrison Central Appraisal District, pay all costs incurred by reason of this appeal.

RENDERED SEPTEMBER 24, 2008
BY ORDER OF THE COURT
JOSH R. MORRISS, III
CHIEF JUSTICE

ATTEST:
Debra Autrey, Clerk

NO. 05-038 1

THE PEOPLE'S GAS LIGHT AND COKE COMPANY,	§	IN THE DISTRICT COURT OF
v.	§	HARRISON COUNTY, TEXAS
HARRISON CENTRAL APPRAISAL DISTRICT,	§	71st JUDICIAL DISTRICT

FINDINGS OF FACT
AND CONCLUSIONS OF LAW

Identification of the Parties

1. Plaintiff is Peoples Gas Light and Coke Company ("Peoples Gas"), a corporation duly formed, organized and existing under the laws of the State of Illinois, with the principal office located at 130 East Randolph Drive, 24th Floor, and Chicago, Illinois and serving retail customers in the Chicago, Illinois area with natural gas.

2. Defendant is Harrison Central Appraisal District ("HCAD"), which is duly organized and acting pursuant to the laws of the State of Texas and is located in Harrison County, Texas.

Pre-Suit Procedural History of the Tax Case:

The Court takes judicial notice of the Stipulations 1-21 and Finds those matters to be Facts as set out in Plaintiff's Proposed Findings of Fact #3-21; and in

the interest of brevity will not set them out again herein.

Peoples Gas and its Business

3. Peoples Gas is a local distribution company responsible for receiving gas from upstream suppliers and delivering it to small residential, commercial and industrial customers within the City of Chicago proper.

4. Peoples Gas maintains no office or employees in Texas, and owns no property in Texas except its ownership of gas it has purchased and is stored in the North Lansing storage facility of NGPL in Harrison County.

5. Peoples Gas contracts with Natural Gas Pipeline of America ("NGPL",) an interstate open access transportation and storage pipeline, for the storage and transportation of natural gas it purchases.

NGPL and its System:

6. NGPL is an interstate pipeline transporting and storing natural gas. Its business of interstate transportation of gas is regulated by FERC. The entire NGPL system will accommodate approximately 250 bcf of gas. But of that amount only a small amount, no more than about 10 to 12 bcf, is located in the pipeline itself. The remainder is located in storage facilities.

7. The NGPL pipeline system in question in this suit consists of two major legs and a "bridge" pipeline

between the two legs. The system forms an inverted "A." The Gulf Coast Leg or Amarillo Leg extends from the southern part of Texas, along the Gulf Coast, through Harrison County, and on through Arkansas, Missouri, and Illinois to the City of Chicago. The Amarillo leg extends from southeastern New Mexico and west Texas through the Texas panhandle, Oklahoma, Kansas, Nebraska, Iowa, and Illinois to the City of Chicago. The "AG line" connects the two pipelines and runs through portions of Oklahoma and Texas.

8. The primary flow of the system is from the southern regions of the United States northward to Chicago. However, along the Louisiana line, from the Texok branch of that line near Houston into Louisiana, gas primarily flows from west to east and in the last several years has flowed exclusively west to east.

9. Gas on the Louisiana leg of the Gulf Coast Line flows primarily east from its intersection with the Gulf Coast Line toward Louisiana, where it may be transferred from the NGPL system to another common carrier for transportation. Under ordinary operating conditions, gas from the Louisiana leg does not reach the North Lansing storage field and gas from the North Lansing storage field does not reach the Louisiana leg.

10. A large portion of the gas on the NGPL system originates in Texas producing fields though it is true that an NGPL customer delivering gas into NGPL's pipelines in New Mexico, arranging transportation

using rights on the Amarillo leg of NGPL's system, and scheduling delivery in Chicago, may actually receive molecules originating offshore in the Gulf of Mexico and transported on NGPL's Gulf Coast Leg. However, due to the nature of the movements on the NGPL system, gas in the North Lansing storage field is very likely produced from the ground in Texas. There is no evidence to indicate that any non-Texas gas is definitively present in the North Lansing storage facility.

The Role of the North Lansing Storage Facility:

11. NGPL uses storage facilities to support the transportation services and to provide storage services to its customers. With respect to the transportation of gas through the system, NGPL adjusts pressures and flow rates in the system to meet the needs that are coming up over the next few hours or days. In order to function properly, the NGPL pipeline must remain full at all times. The volume in the pipeline at any given time is referred to as "line pack". While line pack may be increased or decreased to some degree, the primary capacity of the NGPL system to increase or decrease inventory is in the storage fields. But pipelines can and are operated without storage facilities. The storage rather than transportation function is of greater importance overall. The amount of line pack as of each valuation date was established and detailed in Defendant Exhibit 17.

12. Gas does not flow into and out of NGPL's storage fields while it is in transit through the pipeline. Rather, to put gas into a storage field, it must be taken out of the pipeline and forced under high pressure into the storage field. The storage field is not a just a pipeline of another size. Any gas that is deposited into the North Lansing storage field comes to rest for a business purpose of the owners as well as for NGPL.

13. Due to the unitary and constantly pressured nature of the NGPL system, an amount of gas that is acquired or injected into the system at any point on the system may be delivered at any other point on the system on the same day. The gas which is delivered is not literally the same gas molecules that were acquired, but instead an equivalent number of decatherms.

14. Peoples Gas as well as other NGPL storage customers take advantage of the NGPL storage services to capture the arbitrage value of gas; to ensure adequate supplies of gas in the peak demand cold months; to reduce the need for transportation capacities of gas from the producing areas of the country to the consuming Chicago market area during the typical heating months; and to capture the year-round constant production of gas in a way that will meet the seasonal demand for gas. Peoples Gas typically acquires gas during the warm months of the year, when gas prices are lower, and puts it into storage with NGPL for withdrawal during the cold months of the year when gas prices are higher. Gas

stored to meet seasonal demands of Peoples' customers in a depleted gas reservoir field like the North Lansing facility can be accumulated for as long as the storage customer needs to store its gas with NGPL.

15. In the NGPL system, there are several such storage facilities. These are not manmade but natural underground porous rack formations. Besides the Lansing facility, NGPL owns another depleted gas reservoir storage field located in Sayre, Oklahoma. NGPL also owns several aquifer storage fields, located in the Iowa and Illinois area. Aquifer storage fields are less useful than depleted gas reservoir fields for storing gas because the gas must be cycled in and out of the aquifer storage fields within a few months in order to avoid dissipation of the gas and mixing of the gas with water. An aquifer storage field cannot be used to hold gas for more than a few months at a time. On the other hand, gas can be stored in a depleted gas reservoir, such as the North Lansing storage field, indefinitely without significant risk of dissipation of gas.

16. The North Lansing storage field in Harrison County, Texas is connected to the Gulf Coast Line. It holds approximately 70 billion cubic feet (bcf) of cushion gas. *Cushion gas* is the volume of gas continuously held in the storage field which is necessary to keep the storage field pressurized for delivery. It is not routinely withdrawn from the field unless the reservoir is to be abandoned or retired. The cushion gas is owned by NGPL. The field also contains approximately 83 bcf of working gas. Working gas is the

volume held in the storage field or in the pipeline which is being stored or moved, respectively, on behalf of various customers of NGPL. *Working gas* is not physically separated from cushion gas; the two are commingled in the storage field. The working gas on the NGPL system belongs to the multiple storage customers (or, in some cases, transportation customers) of the NGPL system.

17. The North Lansing Storage Field in Harrison County is the largest capacity storage field on the NGPL system. It is filled nearly to capacity by November 1 of any given year, and the working gas is significantly depleted by April 1 of the following year. The storage capacity of the North Lansing field represents approximately one-third of the entire storage capacity of the NGPL system and more than half of the storage capacity of the Gulf Coast leg.

18. Due to the nature of movements on the NGPL system, gas in the North Lansing storage field is very likely produced from the ground in Texas. There is no evidence to indicate that any non-Texas gas is definitively present in the North Lansing storage field.

The North Lansing Facility and FERC

19. The North Lansing facility is a jurisdictional field regulated by FERC. FERC asserts jurisdiction when they find that the facility is in interstate commerce.

20. The North Lansing facility is a component of the NGPL System, located in the Tex-Ok receipt and delivery zones.

22. NGPL pays property tax on the North Lansing facility's cushion gas, surface facilities, compression treating facilities, wells and gathering systems.

23. In 2002, NGPL applied with FERC for a certificate of public convenience and necessity authorizing NGPL to construct and operate facilities at its North Lansing storage field; FERC made findings that the NGPL proposed construction was in the public interest because it would convert cushion gas into working gas so that NGPL could provide increased storage service on its system; that the proposed facilities, which would provide increased storage service on the NGPL system, would be used to transport gas in interstate commerce; and the proposed facility could appropriately be described as used to transport gas in interstate commerce.

The Business on "Paper":

24. In the NGPL system, the physical molecules of gas themselves come into the system at various points, predominantly in the southern production regions of Texas but also offshore and in New Mexico and then primarily flow northward. The physical location of the gas used to satisfy a customer's demands has no relation to where that customer's gas may be contractually located. NGPL operates its system on a unitary basis: it can supply gas to a customer from any point it chooses to do so.

25. To facilitate the business of buying and transporting, selling and paying, rather than the physical end of transporting physical molecules of gas, the NGPL system is divided into paper storage points and paper pooling points which are designated by unique numbers. Buyers and sellers of gas may trade in gas contractually at paper pooling points and may store gas contractually with NGPL at paper storage points.

26. Paper pooling points and paper storage points do not literally contain the amounts of gas traded or stored at those points. They are an accounting device only and are designated at certain locations in order to facilitate commerce on the NGPL system and to allow NGPL to calculate charges to its customers for transportation and storage services. The paper pooling points or paper storage points where gas is shown to be on NGPL's accounting records bear no relationship to where NGPL chooses to physically store the gas.

27. Each month, NGPL sends each of its customers, including People's Gas, an invoice which details the movements of gas on the NGPL system in the previous month, as well as the stored volumes of gas of that customer. Stored volumes are listed according to their designated contractual paper storage points. The volumes located at the storage points per the invoices do not indicate that *physical* volumes were literally located in the physical area corresponding to the paper storage point.

28. NGPL offers multiple types of storage contracts. The two primary types of storage contracts are DSS (Delivered Firm Storage Service) and NSS (Nominated Firm Storage Service).

29. Delivered [Firm] Storage Service (DSS) is available only in the market area; that is, the area near Chicago, inclusive of the states of Illinois and Iowa. DSS has a transportation component included with it. Gas is available in the market area from a DSS account on demand without any notice from NGPL's customer. DSS accounts are listed contractually as being located in the Iowa-Illinois zone.

30. Nominated Firm Storage Service (NSS) is a storage service which requires the owner to nominate a volume of gas it wishes to have delivered from its storage account with NGPL. Normally, NGPL requires that a nomination be made one day in advance of the customer's desired delivery date. It is available contractually at any paper storage point on the NGPL system.

31. Storing gas under a DSS account is initially considerably more expensive than storing gas under a NSS account. However, if a customer stores gas under a NSS account, it may later have to pay transportation to move the gas to the point where it wishes to take delivery.

32. NGPL does not keep physically separate any of the physical volumes of the gas owned by any of its customers. Customers deposit gas in the NGPL system or acquire gas in the NGPL system and trade

or take delivery of that gas based on a heating unit equivalent known as a decatherm (equal to one million Btu's). Gas from one NGPL location is mixed with other gas in similar locations on the system.

33. The amount of gas that can be delivered out by a storage facility in any given period of time is determined by how full that storage field is. The more full the storage field, the greater the volume of gas it can deliver out. At peak capacity, the North Lansing storage field can deliver one bcf of gas per day.

34. There is no physical storage facility on the NGPL system in the South Texas zone, the Louisiana zone, the Gulf Coast main line zone, the Permian zone, or the Amarillo main line.

35. The North Lansing storage field is proximate to the Texok zone. However, neither North Lansing nor any other storage facility has any contractual connection to the Texok zone or any other zone to- which it may be proximate.

36. Gas shown on NGPL's accounting records to be in a paper storage point in one zone is often physically located in a physical storage field that is not proximate to that zone.

37. Storage customers do not contract for storage in any particular storage field and do not tell NGPL to put gas into any particular storage field. Instead, they contract to have gas in paper storage points in particular zones.

38. Transportation agreements between NGPL and its customers are known as [Firm] Transportation Service agreements (FTS).

39. When a customer acquires gas or introduces gas on the NGPL system, it either markets that gas or deposits the gas into a storage account. If the paper storage point is in the same zone in which the gas was acquired or introduced, the customer does not incur transportation charges. If the paper storage point is in another zone, the customer pays a transportation charge under an FTS agreement to theoretically transport gas to the paper storage point.

40. During 2002 through 2005, Peoples Gas paid transportation charges to NGPL to have the gas it acquired transported to either the Iowa-Illinois zone or the Louisiana zone. This meant that NGPL's accounting records showed Peoples' gas to be stored at paper storage points in those zones. Those records, however, did not reflect the actual *physical* presence of any gas.

41. Even though a storage customer may own gas which is contractually located in the Iowa-Illinois zone and wish to take delivery in the Iowa-Illinois zone on the Gulf Coast leg, that storage customer must, nevertheless, have a FTS agreement with NGPL extending to a point near the North Lansing storage field because it is likely that gas will have to be supplied to the Chicago market area from the North Lansing field.

42. There is insufficient storage field capacity on the NGPL system in the states of Iowa and Illinois to accommodate all of the gas stored in DSS and NSS accounts on the NGPL system.

Benefits to Peoples Gas of the North Lansing Storage Facility:

43. NGPL ultimately utilizes gas withdrawn from the North Lansing storage field in order to satisfy customer needs in the Chicago market area.

44. Peoples Gas benefits from having the gas it has contractually purchased and stored in the North Lansing storage field. Multiple storage fields have enhanced delivery capacity over lesser numbers of storage fields, and geographic diversity of storage fields reduces the possibility of widespread disruption in deliverability due to weather or other natural disasters. Even though customers do not select the physical sites for the storage of gas, they benefit from having NGPL store their gas in the North Lansing storage field.

45. At the beginning of the heating season (around November 1 of each year), approximately 95% of NGPL's storage capacity is generally utilized.

46. The northern storage fields experience productivity declines over the course of the heating season (the cold months), as those fields are depleted and cycled out.

47. Throughout the time frame of 2002 through 2005, Peoples Gas has acquired gas in Texas, at Texas

pooling points, and has maintained FTS agreements with receipt points throughout Texas.

48. Notwithstanding the fact that a specific amount is gas [is] not literally moved from one location to another at the behest of a shipper, the transportation customer pays NGPL as if the purchased gas were moved from the point of receipt to the point of delivery.

49. NGPL anticipates a demand of gas by monitoring the weather in the northern area of its system, particularly the Chicago area. When NGPL anticipates a cold front, it immediately begins moving gas to the Chicago area without waiting for nominations for the same.

50. The relationship between NGPL and its customers is governed by the NGPL tariff and by contracts between NGPL and its customers.

51. Many of the contracts, but not all, between NGPL and Peoples Gas specify Texas as the choice of law governing them.

52. The predecessor or parent company of Peoples Gas built the first gas pipeline from Texas to Chicago in the 1930's. That company owned NGPL and its pipeline and storage system up until 1980, when it sold NGPL to Kinder-Morgan, Inc. The North Lansing storage field was developed by NGPL prior to the time People's Gas sold NGPL to [Kinder-Morgan.]

53. The parent company of People's Gas Light and Coke Company is known as Energy. Other subsidiaries of Energy own gas fields and production in Texas[.]

54. One mcf (thousand cubic feet) of gas on the NGPL system is approximately equal to 0.93 decatherms.

55. NGPL has sufficient storage capacity on its Amarillo leg to accommodate the contractual storage for the Amarillo leg.

56. It is unlikely that any gas from the Amarillo leg is actually physically located in the North Lansing storage field.

Allocation and Calculation Methods and Relationship to Harrison County:

57. Beginning in 1999, in response to the needs of some of its customers, NGPL began preparing allocations regarding ownership of gas at the North Lansing storage field and the Sayre storage field in Oklahoma.

58. The calculation for North Lansing was made by first assuming that all DSS gas was located in the northern storage fields since it has to be immediately available in the Chicago market area. The proportion of ownership of NSS gas in the North Lansing field was then determined by a fraction, the numerator of which is the entire amount of working gas in the North Lansing storage field as of the valuation date, and the denominator of which is the entire amount of NSS gas contractually stored on the Gulf Coast leg.

59. The resulting fraction was then multiplied by the NSS contractual balance of each storage customer on the Gulf Coast leg. Each storage customer then

received a letter from NGPL which detailed the allocated ownership of gas at the North Lansing storage field.

60. As owner and operator of the pipeline system, NGPL is in the best position to know where its customers' gas is physically stored on the NGPL system.

61. The Harrison Central Appraisal District adopted the allocation ownership as determined by NGPL and appraised each owner of NSS gas on the Gulf Coast leg, with the resulting figure attributable to that owner.

62. The allocation method prepared by NGPL and adopted by the Harrison Central Appraisal District indicates that People's Gas owned 2,409,869 mcf of gas as of January 1, 2003 at the North Lansing storage field. The Appraisal District valued that gas at $9,350,290.00.

63. The allocation method prepared by NGPL and adopted by the Harrison Central Appraisal District indicates that People's Gas owned 6,997,012 mcf of gas as of January 1, 2004 at the North Lansing storag[e] field. The Appraisal District valued that gas at $40,498,700.00.

64. The allocation method prepared by NGPL and adopted by the Harrison Central Appraisal District indicates that Gas owned 7,580,674 mcf of gas as of January 1, 2005 at the North Lansing storage field. The Appraisal District valued that gas at $43,816,296.00.

65. Peoples Gas does not care where NGPL physically stores the gas it transports. The concern of Peoples Gas is that gas be delivered to it when and where demanded.

66. Peoples Gas is aware that NGPL utilizes the North Lansing storage facility to meet its system needs.

67. There was a constant presence of a substantial quantity of gas in the North Lansing storage field at all times and throughout 2002 through 2005.

68. Peoples Gas has maintained a constant presence of a substantial quantity of gas in the NGPL system in NSS accounts and derivatively, in the North Lansing storage field, throughout 2002 through 2005.

69. Any gas that is deposited into the North Lansing storage field comes to rest for a business purpose of the owners as well as for NGPL.

70. Harrison County provides services that are substantially related to the taxes it imposes on the gas in the North Lansing storage field. Specifically, Harrison County provides public roads, law enforcement services, health services, public records services, courts, incarceration services, traffic control, and fire suppression services.

71. Hallsville Independent School District encompasses the North Lansing storage field. Hallsville ISD provides services which are substantially related to the taxes it imposes on the gas in the North Lansing storage field. Specifically, it provides free public

education to children and youths of school age within the school district.

72. Harrison County Emergency Services District No. 1 encompasses the North Lansing storage field. The district provides services substantially related to the taxes it imposes on the gas in the North Lansing storage field. Specifically, it provides fire suppression and emergency response services throughout the district. Both it and Harrison County have, on occasion, responded to fires and emergencies concerning gas lines and pumping stations related to the North Lansing storage facility.

73. Since the Harrison CAD appraised only that gas which was actually in the North Lansing storage facility as of January 1 of each year in question, there is no need to allocate any value to other states.

74. A null point exists within the Gulf Coast Leg of the NGPL system. The null point is where the direction of flow switches from one direction to another. There is no evidence that the null point drops south of the North Lancing field.

CONCLUSIONS OF LAW

1. This Court has jurisdiction over Plaintiff's claims for tax years 2003, 2004 and 2005.

2. As of January 1, 2003, 2004 and 2005, the Plaintiff owned substantial quantities of gas in the NGPL system.

3. Throughout 2002 through 2005, there was a constant presence of a substantial quantity of gas in the North Lansing storage field.

4. Throughout 2002 through 2005, People's Gas maintained a constant presence of a substantial quantity of gas in the NGPL system and in the North Lansing storage field.

5. The allocation method determined by NGPL and adopted by the Harrison Central Appraisal District for determining the amount of gas owned by each storage customer at the North Lansing storage field is reasonable and compelling. Gas has not shown that any possible alternative allocation method would be more fair or reasonable.

6. Gas owned by People's Gas in the NGPL system and the North Lansing storage field was at all times in question [system] a quantity of tangible personal property subject to taxation in the State of Texas and Harrison County.

7. The gas owned by People's Gas in the NGPL system, and specifically in the North Lansing storage field, as determined by the allocation method described above, had taxable situs in Harrison County, Texas as of January 1, 2003, 2004 and 2005, in the quantities listed above. The gas was in Harrison County on January 1 of each relevant year for more than a temporary period.

8. At all times during 2002 through 2005, the gas in the North Lansing storage field was not and had not been involved in interstate commerce.

9. Any gas in the North Lansing storage field during 2002 through 2005 which might have at some time been moved in interstate commerce had come to rest as of January 1 of each of those years for the business purpose of the owner, and it was not in actual transportation at that date. It was a part of the general mass of property in Harrison County.

10. Gas owned by "Peoples" Gas in the North Lansing storage field as of January 1, 2003, 2004 and 2005 had a substantial nexus with the State of Texas.

11. The ad valorem taxes assessed on the gas owned by People's Gas at the North [Lansing] storage field do not discriminate against interstate commerce.

12. Since the Harrison Central Appraisal District appraised only gas which was actually located in the North Lansing storage field as of January 1, 2003, 2004 and 2005, there is no occasion for allocating any of the value of that gas to other states or counties.

13. The taxes assessed by Harrison County; Hallsville Independent School District, and Harrison County Emergency Services District No. 1 on the gas at the North Lansing storage field are fairly related to the services provided by those several entities.

14. Even if the gas in the North Lansing storage field was moving in interstate commerce, the taxes on

that gas satisfy the test set out in [*Complete Auto*] *Transport v Brady.*

15. The Plaintiff presented no evidence or legal authority in support of, nor did it ultimately preserve its claim for invalidating the tax at issue herein under the supremacy clause of the United States Constitution.

Signed July 24, 2007

/s/ Bonnie L. Hagan
Judge Presiding

CAUSE NO. 05-0381

PEOPLES GAS, LIGHT AND COKE	§	IN THE DISTRICT COURT
VS.	§	HARRISON COUNTY, TEXAS
HARRISON CENTRAL APPRAISAL DISTRICT	§	71ST JUDICIAL DISTRICT

FINAL JUDGMENT

On January 22, 2007, the above styled and numbered cause of action was called for trial. Both parties announced ready for trial and presented evidence and argument to the Court without a jury, none being requested. The Court, having considered the evidence, arguments and law, finds that judgment should be entered for the Defendant.

IT IS, THEREFORE, ORDERED that the Plaintiff take nothing hereby, that the taxable status as determined by the Defendant on the property that is the subject of this litigation remains unchanged. All costs are assessed against the Plaintiff.

This judgment is final and appealable and resolves all claims and parties brought before the Court. All relief not explicitly granted [herein] is denied.

Signed on this the 1st day of June, 2007.

/s/ Bonnie L Hagan
HONORABLE
BONNIE LEGGAT

[SEAL] OFFICIAL NOTICE FROM
SUPREME COURT OF TEXAS
Post Office Box 12248
Austin, Texas 78711-2248

[POSTMARK MAR 12 2010]

RE: Case No. 09-0053
COA # 06-07-00103-CV
STYLE: HARRISON CENTRAL APPRAISAL DISTRICT
v. THE PEOPLES GAS, LIGHT AND COKE COMPANY

Today the Supreme Court of Texas denied the petitions for review in the above-referenced case.

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[SEAL] OFFICIAL NOTICE FROM
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Post Office Box 12248
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[POSTMARK OCT 01 2010]

RE: Case No. 09-0053
COA #: 06-07-00103-CV
STYLE: HARRISON CENTRAL APPRAISAL DISTRICT
v. THE PEOPLES GAS, LIGHT AND COKE COMPANY

Today the Supreme Court of Texas denied the motion for rehearing of the above-referenced petition for review.

MAIL TO:

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(6)

Supreme Court, U.S.
FILED
MAR 11 2011
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No. 10-896

IN THE

Supreme Court of the United States

HARRISON CENTRAL APPRAISAL DISTRICT,

Petitioner,

v.

THE PEOPLES GAS, LIGHT AND COKE COMPANY,

Respondent.

On Petition for a Writ of Certiorari to the Texas Court of Appeals, Sixth Appellate District

BRIEF IN OPPOSITION

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QUESTION PRESENTED

Whether under the well-settled, multi-factor test set forth in *Complete Auto Transit, Inc.* v. *Brady*, 430 U.S. 274 (1977), a local taxing authority may assess a personal property tax on an out-of-state company engaging in interstate commerce based on a deemed after-the-fact allocation of natural gas temporarily stored in the taxing authority's jurisdiction on a particular day while being shipped interstate, where the company has no contacts with the jurisdiction, cannot control where any gas is stored, has no right to control the disposition of any gas in the jurisdiction, and contracts for its gas to be stored in a different state.

PARTIES TO THE PROCEEDING AND RULE 29.6 STATEMENT

The parties to the proceeding are set forth in the caption.

Pursuant to Sup. Ct. R. 29.6, respondent The Peoples Gas Light and Coke Company states that its parent companies are Peoples Energy LLC and Integrys Energy Group, Inc., and that no other publicly held company owns 10% or more of respondent's stock.

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IN THE

Supreme Court of the United States

No. 10-896

HARRISON CENTRAL APPRAISAL DISTRICT,

Petitioners,

v.

THE PEOPLES GAS, LIGHT AND COKE COMPANY,

Respondent.

On Petition for a Writ of Certiorari to the Texas Court of Appeals, Sixth Appellate District

BRIEF IN OPPOSITION

INTRODUCTION

Petitioner Harrison Central Appraisal District ("the District") asks this Court to correct a purported error by an intermediate state court on a concededly "narrow" issue. Pet. 4, 10, 11. It attempts to justify this request by claiming that the opinion below conflicts with a Supreme Court of Oklahoma decision. This Court declined to review the Oklahoma case only last year, and there is no reason for a different outcome here.

First, just as when the Court denied certiorari in *In re Assessment of Personal Prop. Taxes Against Mo.*

Gas Energy, 234 P.3d 938 (Okla. 2008) ("*Missouri Gas*"), there remains no conflict between state courts of last resort. The Texas Supreme Court has not addressed the issue, and both the Commerce Clause issue and the state law property and tax issues that underlie the federal question therefore remain unresolved in Texas.

Second, as then-Solicitor General Kagan stated in her brief in *Missouri Gas*, there is no conflict as to the governing legal test. Both purportedly conflicting decisions applied the same well-settled test set forth in *Complete Auto Transit, Inc.* v. *Brady*, 430 U.S. 274 (1977). The different results did not stem from disagreement over the federal constitutional test; the courts resolved different factual circumstances relating to different pipelines. In any event, the District seeks only to correct what it perceives as a misapplication of *Complete Auto* to a specific set of facts, which is not a proper basis for certiorari. *See* Sup. Ct. R. 10 ("certiorari is rarely granted when the asserted error consists of * * * the misapplication of a properly stated rule of law").

Third, this Court's review is premature at best because there are independent state law grounds that remain unresolved in Texas. These include the arguments that respondent ("Peoples") lacks any taxable property interest in the gas at issue and that the gas cannot be taxed under Texas law because it is only "temporarily" in the state. The court of appeals did not reach the latter argument in this case, but another Texas court has disallowed a similar tax on that state law ground. If the Texas Supreme Court resolves any of the state law issues against a taxing authority in a future case, that would obviate the constitutional issue in Texas.

Fourth, the court below correctly applied the flexible *Complete Auto* test to "the particular, unique circumstances at hand and the complex relationships among the parties involved." Pet. App. 21. Those unique circumstances include that Peoples has no contacts with Harrison County, no control over the disposition or physical storage of any gas before delivery in Chicago, and no risk of loss should anything happen to any gas in Harrison County. Accordingly, Peoples lacks the requisite nexus with the taxing authority and receives no benefits from taxes paid.

Finally, the case raises no broader issues about the validity of other taxes on other kinds of property. Unlike other circumstances where a party owns taxable property situated in a locality, Peoples lacks any incidents of full title ownership to gas in Harrison County and was simply deemed the technical owner for tax purposes by default. The court of appeals correctly held that these tenuous relationships with the taxing authority were insufficient to permit the tax under *Complete Auto*, and this application of settled law to a narrow factual setting does not warrant this Court's review.

It is not surprising that a Texas locality would try to tax a Chicago business engaged in interstate commerce that has no way to avoid the tax and no legislative recourse. But that is exactly the kind of burden on commerce the Constitution precludes localities from imposing. The petition should be denied.

COUNTERSTATEMENT

A. The Pipeline System.

Peoples is a public utility providing natural gas to over a hundred thousand residential and other

customers in Chicago. 2 Reporter's Record ("RR") 63. It contracts with Natural Gas Pipeline Company of America ("Pipeline") to transport the gas to Chicago. Pet. App. 2.

Pipeline is a common carrier that transports gas on its system pursuant to rates, terms, and conditions regulated by the Federal Energy Regulatory Commission ("FERC"). *Id.* Its pipelines form a tilted "A" on a U.S. map, with two legs that start in Texas and New Mexico, meeting at their northernmost ends (near Chicago), and a connector that crosses through Oklahoma and Texas to join the legs farther up the line. 2 RR 66-67; PX12. Supplies can be injected into the system at various points, which predominantly exist at the southern end. 4 RR 15-16.

Pipeline could not conduct its interstate gas transportation system without storage facilities along the pipelines. 2 RR 42, 147; 3 RR 13. "'Underground gas storage facilities are a necessary and integral part of the operation of piping gas from the area of production to the area of consumption.'" *Schneidewind* v. *ANR Pipeline Co.*, 485 U.S. 293, 295 n.1 (1988) (citation omitted). *See also* 18 C.F.R. § 284.1(a) ("Transportation includes storage, exchange, backhaul, displacement, or other methods of transportation."). Thus, Pipeline must operate the storage facilities both for delivery and operational purposes. 2 RR 30; 3 RR 91, 148-49.

Pipeline has at least eight storage facilities. 2 RR 72. One is in Harrison County, Texas—known as the North Lansing facility—another is in Oklahoma, and six are in the Iowa-Illinois zone. *Id.* FERC determined that the North Lansing facility serves interstate commerce and has asserted jurisdiction over it.

101 F.E.R.C. ¶ 61,361 (Dec. 24, 2002). For its system to work properly, Pipeline must maintain large volumes of "cushion" gas in North Lansing. Pet. App. 2. Pipeline pays substantial ad valorem taxes on this cushion gas as well as its extensive facilities in Harrison County. *Id.* at 22.

This case arises because the District seeks to tax the value of "working" gas, which is part of the interstate shipments of Pipeline's customers. Working gas is injected into and withdrawn from the North Lansing facility for delivery almost daily. 2 RR 148. There is no longer any dispute that this gas is in interstate commerce, as the District has abandoned any claim to the contrary. *See infra* at 11.

B. The Natural Gas Market.

The gas market operates independently from physical transportation systems. Pet. App. 6. A pipeline company's customers do not own particular molecules of gas, or any physical block of gas anywhere on the system. 3 RR 14, 87-99, 95. And Pipeline does not identify particular volumes as belonging to an individual customer. 2 RR 150-51. Indeed, the framework established by FERC separates customer ownership and a pipeline's physical operation—sellers and purchasers may buy and sell at commercial, not physical, points on the pipeline system. 2 RR 34; 3 RR 14, 87-88.

Accordingly, sellers and buyers of gas enter into transactions at commercially-designated points on the system known as paper pooling points. Pet. App. 6. There is no gas physically located at the pooling points. But at the pooling points, customers can trade gas rights, contractually transport gas to the pool, or sell gas to another party. 2 RR 34-35. It is

this latter scenario that applies to Peoples—it delivered no gas into Pipeline's system; instead, all of its natural gas was purchased from other parties at these paper pooling points. 2 RR 88.

Once gas enters Pipeline's system, customers have no control over where in the system the physical gas goes. Rather, "Pipeline decides where and when the natural gas is stored." Pet. App. 7. But customers like Peoples pay to have their gas contractually stored in particular geographic areas. Although Pipeline's contracts with customers do not refer to particular storage fields, they designate storage in specified geographical zones identifying the distance gas is transported for pricing purposes. 2 RR 74, 89-90, 169; PX12. The transportation price is determined by the number of zones between where the gas entered the Pipeline system and where it was delivered. 2 RR 74; PX12. For example, if a producer delivers gas in the South Texas zone and wants to transport the gas to the "TEX-OK" zone, it will be charged more than if it chooses a pooling point in the South Texas zone. 2 RR 74; PX12. However, a customer can only take physical delivery of its gas in the same zone that houses the pooling point for the gas. 2 RR 78-79.

This system compensates for the physical reality that a customer cannot quickly take delivery in Chicago of gas molecules injected into the system elsewhere. 3 RR 94-95; 4 RR 70. While gas may move from South Texas to Chicago the same day for contract purposes—and Pipeline is paid accordingly—the actual molecules of gas could not make it to Chicago in that time, and could ultimately be delivered to any point in the system. 3 RR 94-95.

Thus, even though a customer's supplier might deliver gas produced in Texas into one leg, the customer might receive gas produced in the Gulf of Mexico that was injected by a different supplier into the other leg. 4 RR 73. All that matters is that the gas is delivered in the specified zone. And in light of higher winter demand, Pipeline uses storage to provide greater quantities of gas during that time without having to build other infrastructure. 2 RR 73, 147. Additionally, customers like Peoples purchase gas during the off-season and contractually store that gas on Pipeline's system during the transportation process. 2 RR 105-07.

Peoples' invoices for gas storage evidence that its gas was all stored in the Iowa-Illinois zone. 2 RR 84-88; PX15; PX16; PX17. That is consistent with Peoples' contractual rights, which were limited to storing gas in the Iowa-Illinois zone. 2 RR 89-90. Designating storage in Iowa-Illinois had a significant business advantage for Peoples because it would have cost more if the gas had to cross pricing zones during the more expensive winter months. 2 RR 89.

Peoples is not entitled to any gas located at North Lansing. "[I]t cannot specifically request gas from that facility and could not merely back a truck up to the facility and remove any amount of natural gas." Pet. App. 8. Peoples also has no commercial incidents of ownership over any gas in North Lansing. There is no transaction confirmation or invoice reflecting that Peoples held title to gas located there. Peoples has no legal rights to any gas in North Lansing, faces no risk of loss if anything should happen to the gas there, and has no right to any accretions in the value of the gas in the facility. 2 RR 92; PX21 at 5-6. Indeed, Pipeline must hold

Peoples, and all shippers, harmless for any damage or injuries caused by gas in its system. DX23 at 144. Although Peoples cannot access any gas it purportedly owns in Harrison County, 2 RR 92, it has the right to obtain gas at one of its Chicago-area delivery points in the Iowa-Illinois zone. 2 RR 82, 88.

Peoples' business is providing gas to the people of Chicago. How Pipeline delivers the gas does not concern Peoples and is outside Peoples' control. On the other hand, Pipeline has a significant connection to Harrison County. It owns extensive facilities and 70 billion cubic feet of cushion gas there. 2 RR 169. As a result, Pipeline pays substantial ad valorem taxes to Harrison County on both its facilities and the cushion gas, which Harrison County may use to offset whatever costs it may incur from Pipeline's decision to locate its operations there. Pet. App. 22.

C. The Proceedings Below.

In 1999 and 2000, the District attempted to tax Peoples by allocating it a portion of the working gas balance as of December 31. Peoples challenged the assessments and, on its appraisal consultant firm's advice, the District removed Peoples from the tax rolls. *Id.* at 2-3. The District then changed consultants, and once again attempted to assess taxes against Peoples for tax years 2003 to 2005. *Id.* at 3. This time it refused to remove Peoples from the rolls.

The District allocated gas by first limiting the potential taxpayers to shippers who (1) contracted for transportation on the Gulf Coast Line and (2) had a contract that included a particular form of storage—an NSS contract. *Id.* at 3-4. The District ignored whether contracts included storage in the TEX-OK zone, where Harrison County sits, thereby

including Peoples even though its contracts included storage only in the Iowa-Illinois zone. *Id.* It then determined each remaining shipper's proportion of Pipeline's total NSS contracts for the Gulf Coast Line and multiplied that proportion by the total working gas at North Lansing on December 31 of the preceding year. *Id.*

Peoples protested the assessments, and after a bench trial, the court ruled in the District's favor. In the Texas Court of Appeals, Peoples presented three state law grounds for reversal. First, Peoples argued that it did not own the taxed gas. Br. of Appellant 18-24, No. 06-07-00103 (Tex. Ct. App. filed Dec. 3, 2007). Second, it argued that the District misallocated ownership. *Id.* at 24-26. And third, Peoples argued that the tax was improper under Texas law because the gas only stayed in North Lansing temporarily. *Id.* at 35-37. Peoples also argued that the tax would be invalid under the dormant Commerce Clause. *Id.* at 37-41.

D. The Decision Below.

The Court of Appeals reversed. It noted that while only the property's owner may be taxed under Texas law, "[i]f an individual or entity does not hold perfect legal title * * * that individual or entity may still be considered the taxable owner of the property." Pet. App. 5. The court explained that "[t]he term 'owner' has no fixed legal meaning" and that "'[t]he meaning of the term owner is not the same under all circumstances.'" *Id.* at 6 (citation omitted).

The court then noted facts indicating that Peoples did *not* have perfect legal title, including Pipeline's "full custody, control, and possession of the natural gas," Peoples' lack of any "legal right to the natural

gas located at North Lansing," that Peoples "owns merely contractual rights to physically receive natural gas in Chicago," and Peoples' contracts that "call for contractual storage in the Iowa-Illinois zone." *Id.* at 8. Nevertheless, the court held, by default, that "Peoples is the owner *for ad valorem taxation purposes*," *id.* at 7 (emphasis added), because "there must be an owner of that gas for tax purposes" and, by regulation, it could not be Pipeline. *Id.* at 8.

Next, the court determined that the gas remained in interstate commerce throughout its journey. The court held that the gas became part of interstate commerce when it was placed with Pipeline, a common carrier. *Id.* at 11. And temporarily storing the gas did not remove it from interstate commerce. *Id.* at 12-17.

But this determination only began the Commerce Clause inquiry. The court then applied the settled, multi-factor *Complete Auto* test to determine whether the District could tax the gas even though it was in interstate commerce. Without addressing the remainder of the test, the court invalidated the tax because it failed the first and fourth *Complete Auto* prongs, which require a tax on interstate commerce to be "applied to an activity with a substantial nexus with the taxing state," and "fairly related to the services provided by the State." 430 U.S. at 279.

The court first noted that because Peoples had no physical presence in Harrison County, a nexus could not be established that way. Pet. App. 19. Then, it "look[ed] strictly at the generic act of storing gas in a reservoir in Harrison County." *Id.* The court ruled that storage could not establish a substantial nexus because "Pipeline—not Peoples—directs that activ-

ity," and Peoples' "only connection in this respect to Texas is through the structure and location of Pipeline's pipeline and Pipeline's decision to store a significant amount of natural gas in North Lansing." *Id.* at 20. It found an insufficient nexus due to the "particular, unique circumstances at hand and the complex relationships among the parties involved." *Id.* at 21.

The court ruled, additionally, that the tax failed *Complete Auto*'s fourth prong because services the District purportedly provides, such as police and fire protection, all inure to Pipeline's benefit, not Peoples'. *Id.* at 21-22. It did not rule on Peoples' state law claims that the gas could not be taxed because it was only in the state temporarily or was improperly allocated.

The District petitioned the Texas Supreme Court for review, but abandoned any contention that the gas was not in interstate commerce. In its merits brief to that court, the District stated that it "does not ask this Court to decide the interstate-commerce issue" and that it had "abandon[ed] [this] 'unbriefed' issue." Pet. Brief on the Merits 13, 14, No. 09-0053 (Tex. filed July 6, 2009). *See* Pet. 8 (noting that the taxed gas is "in interstate commerce"). The Texas Supreme Court denied review, Pet. App. 48, and denied a petition for rehearing, *id.* at 49. The District now petitions this Court for a writ of certiorari to review the decision of the Texas Court of Appeals, Sixth Appellate District.

REASONS FOR DENYING THE PETITION

I. THERE IS NO CONFLICT AMONG ANY FEDERAL CIRCUIT COURTS OR STATE COURTS OF LAST RESORT.

The District does not argue that there is a conflict among any state courts of last resort or federal circuit courts that would warrant certiorari under Sup. Ct. R. 10(b). Nor does it allege a conflict between the decision below and any binding precedent of this Court on the question presented. Rather, it identifies a single state supreme court decision that it contends conflicts with the decision of a Texas intermediate appellate court. That lone opinion does not bring this complex issue to a maturity level that warrants this Court's intervention.

Throughout the petition, the District relies heavily on then-Solicitor General Kagan's brief in *Missouri Gas*. But when the Solicitor General recommended denying certiorari—after the opinion below had already issued in this case—she noted that the Oklahoma Supreme Court was "the first and only state court of last resort to have decided whether a State may levy an ad valorem tax on natural gas stored in the State pending transport via an interstate pipeline." Br. for the U.S., *Missouri Gas Energy* v. *Schmidt* ("Invitation Br."), No. 08-1458, at 7 (filed Jan. 26, 2010). For that reason, she stated that the "purported conflicts" between the Supreme Court of Oklahoma and the Texas intermediate appellate courts did not "warrant this Court's review." *Id.*

Nothing has changed. That the District was unable to convince the Texas Supreme Court to take its case is hardly a compelling reason for this Court

to do otherwise. This Court rarely reviews intermediate state appellate court decisions, and no cause exists for such unusual intervention here. As the Court has noted in dismissing a writ of certiorari to an intermediate state court, "[t]he best teaching of this Court's experience admonishes us not to entertain constitutional questions in advance of the strictest necessity." *Parker* v. *Los Angeles Cty.*, 338 U.S. 327, 333 (1949).

There is no such necessity here. As a court of final review, this Court generally allows issues to mature in the lower courts before issuing a nationally binding rule, so that it can benefit from the views of many courts applying the law to various factual scenarios. "[I]t is a sound exercise of discretion for the Court to allow the various States to serve as laboratories in which the issue receives further study before it is addressed by this Court." *McCray* v. *New York*, 461 U.S. 961, 963 (1983) (Stevens, J., concurring in denial of certiorari).

An extraordinary departure from that practice is unwarranted here, where only a single state supreme court has even arguably addressed the issue and review is sought of an intermediate state court decision. As explained below, the courts agree on the governing constitutional test, and the federal question may not even exist in Texas because the Texas Supreme Court may resolve the issue in taxpayers' favor on state law grounds in the future. The District calls the issue "recurring." Pet. 10. If so, this Court can address it if and when a mature conflict develops. If not, there is no reason for this Court to intervene at all.

Just as when the Court denied certiorari in *Missouri Gas*, there remains "no pressing need for this Court's intervention now." Invitation Br. 7. The District cites no exigencies demanding this Court's immediate review without awaiting further opinions from other state courts of last resort or the Texas Supreme Court. Despite its plea of urgency, before 2003 the District itself voluntarily rescinded its tax without judicial invalidation, and it retains the ability to tax the pipeline, its extensive facilities, and cushion gas in the county. Natural gas has been stored underground in this country for nearly a century. Arthur J. Kidnay & William R. Parrish, *Fundamentals of Natural Gas Processing* 256 (2006). Yet the District cites only one case that has ever approved a tax on an interstate shipper's stored gas, and only two appellate cases where the constitutional issue was even considered. There is no more reason for this Court to intervene now than when the Court denied certiorari in *Missouri Gas*.

II. THERE IS NO DISPUTE OVER THE PROPER LEGAL STANDARDS.

No conflict exists between the Texas Court of Appeals and the Oklahoma Supreme Court over the correct legal standards. Both courts applied the same standard mandated by this Court: the *Complete Auto* test. *Compare* Pet. App. 18 *with Missouri Gas*, 234 P.3d at 952-59. At best from its perspective, the District complains about "the misapplication of a properly stated rule of law," which is not a proper basis for certiorari. Sup. Ct. R. 10. *See* DCAD Amicus Br. 10 (arguing that "the Court of Appeals simply applied the *Complete Auto* test to the facts at hand incorrectly").

1. Because it cannot dispute that the two courts applied the same legal test, the District attempts to manufacture a controversy over whether and to what extent a "continuity of transit" or "physical presence" analysis supersedes the *Complete Auto* test in cases like this. Pet. 14-20. No such controversy exists.

With regard to the "continuity of transit" analysis, the Solicitor General correctly explained that the court below did not apply that analysis in lieu of--or even as part of—the *Complete Auto* test. She stated that "various state courts"—specifically including the Texas Court of Appeals in this case—"have applied the *Complete Auto* factors, *rather than the 'continuity of transit' test*, in adjudicating dormant Commerce Clause challenges to local taxation." Invitation Brief 11 (citing opinion below; emphasis added).

The court below referred to the "continuity of transit test" only as a hurdle for *Peoples* to overcome *before* the *Complete Auto* test could be applied. Pet. App. 16-17. It used the test to determine whether the gas remained in interstate commerce, as a pre-requisite for applying *Complete Auto*. *Id.* If no continuity of transit had been shown, the tax would have been upheld on that ground.

Contrary to the District's claim that the analysis colored all the court's subsequent analysis, Pet. 16, the court never addressed the continuity-of-transit test again. Instead, it independently applied the *Complete Auto* test to determine whether the tax was valid even though it was in interstate commerce. Pet. App. 18-21. To the extent the Oklahoma Supreme Court believed the Texas Court of Appeals applied the continuity-of-transit analysis in lieu of *Complete Auto*, *see Missouri Gas*, 234 P.3d at 959

n.84, the court misread the opinion in this case. Accordingly, the purported "direct conflict" between the courts on this point, Pet. 16, is a false one.

Indeed, by independently applying the *Complete Auto* test without considering the continuity-of-transit factors under that test, the court below employed an analysis that was more favorable to the *District* than it had to be. As the Solicitor General noted, "[i]n cases like this one, the same factors that the Court previously considered to determine continuity of transit may inform the first prong of the *Complete Auto* inquiry." Invitation Brief 12. Thus, while it would have been appropriate for the court to employ the continuity-of-transit factors under the *Complete Auto* test—which would have weighed against the District—it did not.

Nor is there any conflict over the "physical presence" test. Applying the first prong of *Complete Auto*—whether a substantial nexus exists—the court below first noted that "[t]he Commerce Clause requirement of a substantial nexus with the taxing state is satisfied by the taxpayer's physical presence in the state." Pet. App. 19. Unsurprisingly given the lack of contacts between Peoples and Harrison County, the court found no such presence. But the court did not suggest that physical presence was the *only* way to establish a substantial nexus. It merely concluded that Peoples' lack of a physical presence meant that some other nexus must exist.

Contrary to the District's suggestions, Pet. 18-20, the court did not stop there. It then analyzed the nexus issue "look[ing] strictly at the generic act of storing gas in a reservoir in Harrison County," Pet. App. 19—exactly what the District advocates here,

Pet. 25-26. The court also analyzed whether a nexus could be established based on a claim that the gas comes from Texas. Pet. App. 20. Finding that no proffered rationale established a substantial nexus, the court held that the tax failed *Complete Auto*'s first prong. As with the continuity-of-transit analysis, the court's finding of no physical presence neither supplanted nor dictated the outcome of the *Complete Auto* test.

2. The different result in *Missouri Gas* did not stem from disagreement over the applicable legal test but rather from applying that test to similar, but nonetheless distinct, facts.

For example, in finding a substantial nexus, the Oklahoma court held that the shipper could not argue that it did not intend for storage to occur in Oklahoma on the facts of that case. *Missouri Gas*, 234 P.3d at 955 ("If gas is stored [in Woods County], and it is, MGE cannot claim it does not intend for that to happen."). Indeed, the taxpayer offered no evidence that it did not own the taxed gas. *Id.* at 951. Moreover, the Oklahoma court (and the Solicitor General) found it significant that FERC had approved a tariff establishing an apportionment formula for gas stored in the facility, which helped prevent any undue burden on interstate commerce. *See id*; Invitation Br. 3, 6-7, 17, 18, 20. The court also noted that all of the gas at issue "originates within the state of Oklahoma." *Missouri Gas*, 234 P.3d at 949. And based on the facts of that case and Oklahoma law, the court held that the shipper had "unified title"—both legal and beneficial—to a share of the gas stored in Oklahoma. *Id.* at 948.

Here, by contrast, there can be no claim that Peoples affirmatively intended for storage to occur in Harrison County. To the contrary, the only indicia of Peoples' intent are contracts that expressly call for storage in the Iowa-Illinois zone, and invoices confirming that contractual storage. 2 RR 84-88, 89-90; PX15; PX16; PX17. Unlike in *Missouri Gas*, there is no FERC-approved allocation here evidencing shippers' understanding that their gas would be allocated to a Texas situs. Likewise, although the record "suggests" that much of the gas at North Lansing was Texas-produced, the origination of gas that Peoples purchased off of Pipeline's system can never be known. Pet. App. 21. And the Texas court, applying Texas law, did not hold that Peoples had full, unified legal title to any gas in Harrison County. Rather, it held only that Peoples was the owner, by default, "for ad valorem taxation purposes," *id.* at 7, based solely on its conclusion that Pipeline could not be the owner, *id.* at 8-9. In contrast to the Oklahoma court's holding under that state's law that shippers have full, unified title to gas stored in Oklahoma, under Texas law Peoples "has no legal right to the natural gas located at North Lansing." *Id.* at 8.

Moreover, the Oklahoma Court held that the gas at issue in that case was "not in transit in such a way as to invoke the protection of the Commerce Clause." *Missouri Gas*, 234 P.3d at 955. Although the Texas Court of Appeals reached a different conclusion on this threshold issue on the facts of this case, the District expressly abandoned that argument in the Texas Supreme Court and does not present it in its petition to this Court. *See supra* at 11. Accordingly,

any conceivable conflict between the courts on this threshold issue is not before this Court.

Furthermore, the Oklahoma court reviewed circumstances under which the shipper had purchased natural gas from suppliers and contracted with the pipeline for transportation of that gas once the gas was placed on the system. *Missouri Gas*, 234 P.3d at 943, 944. By contrast, all gas purchased by Peoples was already in transport on Pipeline's system and purchased at paper pooling points. 2 RR 88.

In the end, the Texas court found no substantial nexus given "the particular, unique circumstances at hand and the complex relationships among the parties involved." Pet. App. 21. The Oklahoma court quoted this language in reaching a different result on the facts before it. *Missouri Gas*, 234 P.3d at 959 n.84. Although that court disagreed with what it thought was the reasoning of the court below, *id.*, much of that disagreement stemmed from misreading the opinion. As noted above, *supra* at 15-16, the Texas Court of Appeals did not employ the continuity-of-transit analysis to determine that the tax failed the *Complete Auto* test.

III. THERE ARE DISPOSITIVE, INDEPENDENT, UNRESOLVED STATE LAW GROUNDS.

Review is also premature because significant, independent state law grounds remain unresolved in Texas that could—and likely would if later considered by the Texas Supreme Court—render advisory any decision by this Court on the constitutional question. *Cf. Parker*, 338 U.S. at 332 (where California Supreme Court denied review, certiorari to intermediate state court was inappropriate because "[f]or all we know the California courts may

sustain these claims under local law"). Nor should the Court consider the constitutional issue without a definitive ruling on the state law questions that underlie proper consideration of the nexus issue.

1. Under Texas law, personal property tax may only be assessed against property located in the taxing unit for more than "a temporary period." Tex. Tax Code § 11.01(c)(1). The statute does not define "temporary," which is left to judicial construction on the facts of each case. *Patterson-UTI Drilling Co.* v. *Webb Cty. Appraisal Dist.*, 182 S.W.3d 14, 18 (Tex. App. 2005). Property is in a jurisdiction only "temporarily" if it is not there with a "degree of permanency." *Greyhound Lines, Inc.* v. *Bd. of Equalization*, 419 S.W.2d 345, 349 (Tex. 1967).

Under Texas law, personal property is in the state only temporarily if it is in interstate commerce. *See Dallas Cty. Appraisal Dist.* v. *L.D. Brinkman & Co.*, 701 S.W.2d 20, 23 (Tex. App. 1985). Such property is not taxable under state law, *id.*, regardless of whether the Commerce Clause would also prohibit the tax. There is no longer any dispute that the gas at issue remains in interstate commerce. The Texas Court of Appeals so held, Pet. App. 17, and the District abandoned any appeal of that conclusion in the Texas Supreme Court, *supra* at 11. The argument has therefore been waived both in this Court and in Texas. *See Parker* v. *Illinois*, 333 U.S. 571 (1948); *Guitar Holding* v. *Hudspeth Cty. Underground Water Conservation Dist. No. 1*, 263 S.W.3d 910, 918 (Tex. 2008) ("issues not presented in the petition for review and brief on the merits are waived").

Peoples expressly argued, both to the Court of Appeals and to the Texas Supreme Court in a

conditional cross-petition for review, that the gas could not be taxed under Texas law because it was only temporarily in Harrison County. *See* Br. of Appellant 35-37, No. 06-07-00103 (Tex. Ct. App. filed Dec. 3, 2007); Resp. Br. on the Merits 53-55, No. 09-0053 (Tex. filed Aug. 10, 2009). The Court of Appeals did not reach this argument, and the Texas Supreme Court had no occasion to do so because it denied review.[1] But based on the precedents cited above, it is likely the Texas Supreme Court would hold that Texas state law prohibits taxation of gas stored while being shipped in interstate commerce.

Indeed, one Texas court has already so held in a similar case. In *Midland Cent. Appraisal Dist.* v. *BP Am. Production Co.*, 282 S.W.3d 215, 225 (Tex. App. 2009), a case that the District claims raises similar issues to this case, Pet. 17-18, the Court ruled as an alternative, independent state ground that the appraisal district could not assess personal property taxes on oil in a tank farm because the oil was only in Texas temporarily.

Because a determination that the gas is in interstate commerce precedes any consideration of the Commerce Clause defense, such a state-law holding by the Texas Supreme Court would obviate the federal issue. Accordingly, this Court should not render what would likely become an advisory opinion on a constitutional issue where the Texas Supreme Court has not yet ruled on whether Texas law even permits this kind of tax.

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[1] In the unlikely event this Court grants certiorari and reverses on the federal issue, Peoples could, on remand, re-petition the Texas Supreme Court on this and other state law defenses.

2. Peoples also argued below that it could not be taxed on any gas in Harrison County because it was not the owner of that gas under Texas law. Although the Texas Court of Appeals rejected that argument, Peoples reasserted that state-law defense in its conditional cross-petition to the Texas Supreme Court. *See* Resp. Br. on the Merits 16-22, No. 09-0053 (Tex. filed Aug. 10, 2009). Because it denied review, that court did not decide the issue.

The extent of Peoples' ownership interest, if any, in the taxed gas undergirds the judgment the District asks this Court to review because the purported nexus between the county and the taxpayer depends in part on the nature of that interest. Yet there is no definitive ruling on that issue by the final arbiter of Texas law. As with the "temporary period" question, if the Texas Supreme Court later rules on this issue in a taxpayer's favor, that would eliminate any need to consider the federal question. Moreover, a definitive understanding of the property interest (if any) is crucial to any intelligent analysis of the Commerce Clause nexus, particularly given the District's contention that an alleged property right is dispositive of the question. This Court should not prematurely review the federal question where the Texas Supreme Court has not yet spoken on that important state-law issue. *See Tyler Pipe Indus., Inc.* v. *Wash. State Dept. of Rev.*, 483 U.S. 232, 252 (1987) (declining to consider Commerce Clause refund issues where "'the federal constitutional issues involved may well be intertwined with, or their consideration obviated by, issues of state law'") (citation omitted).

3. Peoples also argued below that the District's allocation violated Texas state law, and that under a

proper allocation Peoples should not have been allocated any gas in Harrison County. *See* Br. of Appellant 24-26, No. 06-07-00103 (Tex. Ct. App. filed Dec. 3, 2007). To allocate the gas for tax purposes, the District excluded shippers based on what kind of storage they contracted for and which leg of the pipeline their contracts specified, Pet. App. 3-4, even though the pipeline works in the aggregate and thus gas physically stored in Harrison County is delivered to both excluded classes, 2 RR 32-33, 46. This artificially increased the amount of gas allocated to shippers like Peoples. Had the District applied a consistent and proper allocation, it could not have allocated any ownership to Peoples, which contracted for storage in a different zone.

The Court of Appeals did not specifically address this issue and neither, of course, has the Texas Supreme Court. In considering the federal constitutional issue, it is plainly important to know whether any gas is properly allocated to Peoples under state law and, if so, how much. As with the other state-law issues, this Court should not prematurely review that constitutional issue where the allocation question remains unresolved under Texas law.

IV. THE DECISION BELOW IS CORRECT.

Although certiorari is unwarranted in any event, the court below did not err in applying the flexible, four-factor *Complete Auto* test to "the particular, unique circumstances at hand." Pet. App. 21.[2]

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[2] Nor did Solicitor General Kagan opine otherwise in her advocacy role in *Missouri Gas*. She merely stated that the Oklahoma court reached the correct result in that case "based on the record below" and "[b]ased on the current record." Invitation Br. 6, 13. When referring to the decision in this case, she noted

1. The Texas Court of Appeals did not err in holding that the District failed to meet the first prong of the *Complete Auto* test. It is now conceded that the gas at issue is in interstate commerce. *See supra* at 11. Thus, to be valid, the District's tax must be "applied to an activity with a substantial nexus with the taxing state." *Complete Auto*, 430 U.S. at 279. Harrison County is trying to tax *the shipper*—Peoples—not the gas, which is an inanimate substance incapable of receiving or paying a tax bill. Thus, there must at least be a definite link between the shipper and the property to be taxed as well as between the property and the county. As the Court of Appeals correctly found, no such substantial nexus exists here because Peoples lacks any significant ties to any gas in Harrison County. It only has a contractual right to take gas in interstate commerce that was stored in the Iowa-Illinois zone.

The court below found that Peoples, by default, had a technical ownership interest in gas in Harrison County for tax purposes. Pet App. 7. But it recognized that this technical interest did not amount to a property right or full title ownership. *Id.* at 8. Peoples does not have full legal title under Texas law in light of (1) Pipeline's "full custody, control, and possession of the natural gas," (2) Peoples' lack of any "legal right to the natural gas located at North Lansing," (3) the fact that Peoples "owns merely contractual rights to physically receive natural gas in Chicago," and (4) the fact that Peoples' contracts "call for contractual storage in the Iowa-Illinois

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only a "purported conflict[ ]" and indicated that the Texas Court of Appeals had applied the *correct* legal test. *Id.* at 7, 11.

zone." *Id.* And without such legal title, there is no way to establish a nexus between the taxed entity and Harrison County merely through the location of the taxed property. *Id.* at 19-21.

Nor can a nexus with Harrison County be established through any actions undertaken by Peoples. Because Peoples has no physical presence there—or anywhere in Texas—in the form of offices, employees, representatives or facilities, a nexus cannot be established that way. *Id.* at 19. Pipeline, not Peoples, controls the gas before delivery in Chicago, and Pipeline alone bears the risk of loss should anything happen to gas in Harrison County. *Id.* at 8. Peoples does not intend to store, use or sell gas within Texas. Indeed, Peoples cannot even access any gas in Harrison County and its contracts specify storage elsewhere. Nor does storage in Harrison County serve any business purpose of Peoples. Indeed, its business would be impeded by storing gas there because it would make delivery during the winter months more expensive, which is why it contracts for storage in the Iowa-Illinois zone. 2 RR 89. Unlike in *Missouri Gas*, there is no evidence that all gas attributed to Peoples originated in Texas. Pet. App. 21. And the State has already addressed beneficial use of gas originating in Texas through its severance tax and tax on gas reserves. Tex. Tax Code §§ 201.051, 23.175.

The District concedes that "volumes of Peoples' gas may come and volumes of gas may go," because it is subject to near-constant movement. Pet. 26. Thus, the District seeks to establish a substantial nexus based on a fictional allocation of gas moving in interstate commerce on a particular day according to variables in existence on that day alone, where the

technical owner has no ability to avoid the tax by specifying storage elsewhere, no rights to the property, and no legislative representation in the taxing jurisdiction. Given these "particular, unique circumstances at hand and the complex relationships among the parties involved," Pet. App. 21, the court below did not err in finding no substantial nexus.

Moreover, although the Court of Appeals did not employ a continuity-of-transit analysis in applying the *Complete Auto* test, that analysis, as the Solicitor General has noted, can be used to "inform the first prong of the *Complete Auto* inquiry." Invitation Br. 12. If a product is merely passing through a state in interstate commerce to be sold in another state, any link to the state it transits is minimal and any tax on it is unlikely to survive scrutiny under *Complete Auto*. Thus, if those factors are added to the equation in this case, the invalidity of the tax becomes even clearer. *See* Pet. App. 12-17 (applying continuity-of-transit analysis to determine that the gas remains in interstate commerce). Indeed, the District has abandoned any argument that the gas in question does not remain in interstate commerce, resting instead on its position that the continuity-of-transit analysis is wholly irrelevant.

The District essentially advocates for elimination of the nexus requirement for all *ad valorem* property taxes. It finds it irrelevant whether property is only temporarily in a jurisdiction as part of an interstate journey or whether the technical owner has any presence in the jurisdiction or right to control whether the property is even there. Instead, it contends that the location of property moving in interstate commerce on a particular "tax day" alone justifies the tax. *See* Pet. 26. If so, there is no rea-

son why a locality could not tax the value of anything in interstate commerce that happens to be in the jurisdiction on tax day, be it gas moving through a pipeline or FedEx packages in an overnight sorting facility. Although the District disclaims that result, *id.* at 27, nothing in its simplistic location-of-the-property test would limit such taxes.

2. Nor did the Court of Appeals err in holding that the tax independently fails *Complete Auto*'s fourth prong because Peoples receives no benefits from Harrison County. The fourth prong is related to the first, but "imposes the additional limitation that the *measure* of the tax must be reasonably related to the extent of the contact, since it is the activities or presence of the taxpayer in the State that may properly be made to bear a 'just share of the state tax burden.'" *Commonwealth Edison Co.* v. *Montana*, 452 U.S. 609, 626 (1981) (citation omitted; emphasis in original). "When a tax is assessed in proportion to a taxpayer's activities or presence in a State, the taxpayer is shouldering its fair share of supporting the State's provision of 'police and fire protection, the benefit of a trained work force, and 'the advantages of a civilized society.'" *Id.* at 627 (citation omitted).

Peoples has no "activities or presence" in Harrison County. It has no physical presence, and the only purported link it has is the taxed gas. But Peoples is only the nominal, default owner "for tax purposes." Pet. App. 8. It does not choose to store gas in Harrison County or invoke any of its protections. *Id.* at 20. And most importantly, Peoples bears no risk of loss from anything that happens to the gas in Harrison County.

The only service the District raises as beneficial to Peoples is "the need for fire protection." Pet. 29. But because Peoples has no risk of loss, it does not benefit from fire protection—Pipeline does. Nor does Peoples benefit from police protection, a trained work force in Harrison County, or any other government activity. All benefits of a civilized society provided by Harrison County inure to the benefit of Pipeline. Pet. App. 21-22 ("services such as law enforcement and the fire department would serve the North Lansing facility itself, and the facility undoubtedly belongs to Pipeline"). And that is why Pipeline legitimately is required to pay taxes on its facility and on the cushion gas. *Id.*

The District claims that Pipeline's role and taxes paid are irrelevant because "Peoples' working gas" should be taxed. Pet. 28 (emphasis omitted). But even assuming that Peoples has working gas in Harrison County, the fact that it bears no risk of loss means that it gains no benefit from whatever protection Harrison County provides.

3. Although the Court of Appeals did not need to address *Complete Auto*'s second prong, the District's tax fails that requirement as well. Indeed, the lack of any opinion below on that issue is yet another reason why this Court's review would be premature.

Complete Auto's second prong requires a tax to be fairly apportioned. To be fairly apportioned, a state's tax on goods in interstate commerce must be both "internally and externally consistent." *Goldberg* v. *Sweet*, 488 U.S. 252, 261 (1989). A tax is externally consistent if "the State has taxed only that portion of the revenues from the interstate activity which reasonably reflects the in-state component of the

activity being taxed." *Id.* at 262. "[T]he threat of real multiple taxation (though not by literally identical statutes) may indicate a State's impermissible overreaching." *Okla. Tax. Comm'n* v. *Jefferson Lines*, 514 U.S. 175, 185 (1995).

The District has created a clear threat of multiple taxation; indeed, Peoples could be taxed on the same gas several times over. Unlike the taxing authority in *Missouri Gas*, the District did not follow a FERC-approved allocation, but rather allocated gas in Harrison County to all customers with NSS contracts on the Gulf Coast line, excluding those shipping on the other line and those with other types of storage contracts. But because nobody can ever know where a shipper's gas molecules are actually located, another taxing authority might allocate tax liability among all shippers who "own" gas on the entire system as a whole, including a share already taxed by Harrison County. If a jurisdiction on Pipeline's other line adopted that formula, Peoples would be taxed on gas purportedly stored both in Texas and the other state simultaneously. Moreover, if a jurisdiction in the Iowa-Illinois zone chose to allocate ownership based on where the parties actually agreed to store the shipper's gas, Peoples would be taxed *again* on the same gas because *all* of its gas is stored contractually in the Iowa-Illinois zone. And if different jurisdictions use different "tax days," shippers like Peoples could pay multiple taxes on the same gas as storage allocations continually change on ensuing days.

Thus, the District's tax fails *Complete Auto*'s second prong because there is a threat that Peoples will be taxed multiple times on the same gas. *Cf. Michigan-Wisconsin Pipe Line Co.* v. *Calvert*, 347 U.S. 157, 170

(1954). Nor is it relevant that this harm has not yet come to pass, because the threat of multiple taxation itself suffices to invalidate the tax. *See Tyler Pipe Indus., Inc.* v. *Wash. State Dep't of Revenue*, 483 U.S. 232, 242 (1987) (unconstitutionality of tax "cannot be alleviated by examining the effect of legislation enacted by its sister States"); *Armco, Inc.* v. *Hardesty*, 467 U.S. 638, 645 (1984) (invalidity does not "depend on the shifting complexities of the tax codes of 49 other states").

4. The Commerce Clause arose from the Framers' "conviction that in order to succeed, the new Union would have to avoid the tendencies toward economic Balkanization that had plagued relations among the Colonies and later among the States under the Articles of Confederation." *Hughes* v. *Oklahoma*, 441 U.S. 322, 325 (1979). It prevents "state taxes and regulatory measures [from] impeding free private trade in the national marketplace." *Reeves, Inc.* v. *Stake*, 447 U.S. 429, 437 (1980).

The tax at issue threatens just this kind of harm to commerce. If every locality may tax the value of a commodity that is concededly in interstate commerce and over which the technical owner has no control, the burdens on commerce would multiply with every locality the commodity crosses. Out-of-state entities like Peoples, which have no connection with the taxing authority and no ability to avoid the tax, would be easy marks. And every jurisdiction would enact their own retaliatory tax. *Cf. Nat'l Private Truck Counsel* v. *Okla. Tax Comm'n*, 515 U.S. 582, 584 (1995). States and their subdivisions would be forced to negotiate tax rates and bilateral trade agreements with each other on essential fuels as if they were foreign sovereigns, and they could "drift

toward anarchy and commercial warfare." *H.P. Hood & Sons* v. *Du Mond*, 336 U.S. 525, 533 (1949). "Avoiding this sort of 'economic balkanization,' and the retaliatory acts of other States that may follow, is one of the central purposes of [this Court's] negative Commerce Clause jurisprudence." *Camps Newfound/Owatonna, Inc.* v. *Town of Harrison*, 520 U.S. 564, 577 (1997) (citation omitted).

Given the unique facts of this case, the court below correctly held that a Texas taxing authority cannot tax Peoples—which effectively becomes a tax on citizens of Chicago who have no connection with the jurisdiction and no redress at the polls—by levying a tax on the value of a commodity concededly in interstate commerce. That fact-intensive ruling by an intermediate state appellate court does not warrant this Court's extraordinary intervention.

V. THIS CASE IMPLICATES NO BROADER CONCERNS ABOUT TAXES ON OTHER KINDS OF PROPERTY.

The ruling below will not have the broader effects the District "envisions." Pet. 19-20. The District wrongly contends that this case implicates the validity of other "real or personal property" taxes levied on entities without a physical presence in the jurisdiction. *Id.* at 20.

Because real estate never moves in interstate commerce, the issues in this case are irrelevant to such taxes. And taxes on other kinds of property will almost always have a greater nexus than exists here, because one will be able to identify an owner who has at least some control over what happens to the property. As explained above, the Texas Court of Appeals did not hold that physical presence was a

prerequisite to finding a substantial nexus, only that another nexus must exist where physical presence is lacking. It found no such nexus given the virtually unique circumstances of a party that was deemed the technical owner by default of an untraceable, allocated portion of a commodity moving in interstate commerce over which the party has no control. Tangible personal property is rarely so fungible and intermingled as to involve imputing ownership to a party that has no control over the property and no right to access it, and that specifically contracted to place the property elsewhere.

In its petition, the District asserts that this purportedly broader question implicated by this case was presented in another petition involving whether the "physical presence" test applies only to sales and use taxes. Pet. 20 (citing *Asworth, LLC* v. *Dep't of Rev., Finance, & Admin. Cabinet*, No. 10-662). Since then, the Court has denied certiorari in *Asworth*. Given that certiorari was not warranted when this broader issue was directly presented, it clearly is not warranted here.

The District and its amici also overstate the breadth of the issue even as it affects natural gas and oil. Amici imply that localities are clamoring to enact such taxes. But since *Complete Auto*, reported decisions in only three states (Oklahoma, Texas and Kansas) have addressed localities' attempts to tax gas or oil stored as part of interstate shipments. *Cf. In re Appeal of the Dir. of Prop. Valuation*, 161 P.3d 755 (Kan. 2007) (disapproving tax on state law grounds). If such a groundswell does appear, and if state courts of last resort eventually conflict on the

issue, the Court can visit the issue then.[3] Even in Oklahoma, however, the issue is narrowly limited to gas originating within that state. In *Missouri Gas*, 234 P.3d at 948-49, 963, the court held that Oklahoma state law would preclude a tax on any gas that originated outside of the state. And as noted above, it is likely that Texas precludes such taxes on numerous state law grounds.

Moreover, in some cases the issue might be resolved on the ground—no longer contested here—that particular gas supplies are not moving in interstate commerce. During the years at issue, North Lansing was the only Texas storage field over which FERC asserted regulatory jurisdiction, 3 RR 147, and it is currently one of only two operating FERC jurisdictional gas fields in the state, *see* FERC, *Jurisdictional Storage Fields in the United States by Location* (www.ferc.gov/industries/gas/indus-act/storage/fields-by-location.pdf). It remains to be seen how the constitutional question would be resolved as to the many other non-jurisdictional fields.

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[3] Recently, a Kansas administrative body ruled on the taxation of stored gas without reaching federal constitutional issues. *See In re Appeals of Various Applicants from an Order of the Dir. of Prop. Valuation*, No. 2009-8554-PV (Kan. Ct. Tax App. Feb. 17, 2011). If that case is litigated further, and if a decision reaches those issues and burdens interstate commerce, the Court would also be able to visit the issue then. *Cf.* Invitation Br. 20-21 (future case could be ripe for review "if facts come to light indicating that such taxes cause a significant disruption in the interstate transport of natural gas or that they cannot be assessed in a fair and non-discriminatory manner").

CONCLUSION

For these reasons, the petition should be denied.

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In The
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HARRISON CENTRAL APPRAISAL DISTRICT,

Petitioner,

v.

THE PEOPLES GAS, LIGHT AND COKE COMPANY,

Respondent.

On Petition For A Writ Of Certiorari To The Texas Court Of Appeals, Sixth Appellate District

REPLY BRIEF FOR PETITIONER

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REPLY BRIEF FOR PETITIONER

The now-ripe constitutional conflict implicated in this case is important and recurring: The conflict is due to differing constitutional analyses, not – as Peoples claims – to factual distinctions. The various state-law issues that Peoples raises were either expressly rejected by the court below or not reached, and therefore constitute no obstacle to this Court's review. This Court should address the question squarely presented, without further delay.

I. The constitutional issue presented is important and recurring, and the conflict should be resolved without further delay.

When faced with the unfavorable Oklahoma decision in *Missouri Gas*, the gas industry argued that the constitutional question presented in that case – which is the same as that presented in this one – is "a recurring issue that merits this Court's attention." Am. Gas Ass'n Amicus Br. (No. 08-1458), at 3. Just last Term, Missouri Gas argued that review "is urgently needed." Pet. Rhrg. (No. 08-1458), at 3. This Court took those arguments seriously, inviting the Solicitor General to express the views of the United States, even in the absence of a conflict between the decision at issue in that case and any decision of a state court of last resort or federal court of appeals.

The Solicitor General urged this Court to deny review, not because the issue is unimportant, but

because "[t]he Oklahoma Supreme Court applied the correct legal standard and, based on the record below, reached the correct result." U.S. Br. (No. 08-1458), at 6. The recognized conflict between the *Missouri Gas* decision and the decision below did not warrant review at that time, but only because "[t]he Texas Supreme Court" was then "in the process of deciding whether to grant further review," *id.*, at 7 – which it has now denied. And review of a decision *upholding* an ad valorem tax against constitutional challenge was also unnecessary "because FERC has authority to disapprove a tariff specifying an objectionable allocation formula." *Id.*, at 6-7, 20-21. The same rationale does not apply to a decision *striking down* a tax.

Now that, just one year later, the gas industry enjoys a final, favorable Texas decision, Peoples argues that this ripe conflict should percolate indefinitely among the state courts. It should not. Review is even more urgently needed now because the very real conflict creates illogical distortions in the taxation of natural gas among the various States and as between intrastate and interstate gas, and encourages costly litigation.

Peoples does not dispute that this constitutional issue is recurring. And the importance of the issue is confirmed by the amicus briefs supporting the gas industry in *Missouri Gas* and the amicus briefs supporting the Appraisal District in this case.

Peoples also argues that the Court should decline review because the challenged decision is from an intermediate state court. Br. Opp., at 13. That should not dissuade the Court. The Court frequently grants review of decisions by state intermediate courts of appeals. *See, e.g., Goodyear Dunlop Tire Operations, S.A. v. Brown*, No. 10-76 (argued Jan. 11, 2011) (pending); *Graham v. Florida*, ___ U.S. ___, 130 S. Ct. 2011 (2010); *Norfolk Southern Ry. v. Sorrell*, 549 U.S. 158 (2007); *Hudson v. Michigan*, 547 U.S. 586 (2006); *Mid-Con Freight Systems, Inc. v. Michigan Pub. Serv. Comm'n*, 545 U.S. 440 (2005); *American Trucking Ass'ns, Inc. v. Michigan Pub. Serv. Comm'n*, 545 U.S. 429 (2005); *Lawrence v. Texas*, 539 U.S. 558 (2003); *Arizona Dep't of Rev. v. Blaze Constr. Co.*, 526 U.S. 32 (1999). Also, this Court has not hesitated to review a dormant Commerce Clause decision, like this one, by a state intermediate court of appeals. *See American Trucking Ass'ns, Inc. v. Michigan Pub. Serv. Comm'n*, *supra*; *D.H. Holmes Co. v. McNamara*, 486 U.S. 24, 29, 31 (1988) (deciding whether State's imposition of use tax on catalogues printed outside of State, but shipped into State, violated dormant Commerce Clause, by reviewing decision of Louisiana Court of Appeal after Louisiana Supreme Court denied discretionary review).

As the gas industry argued in *Missouri Gas*, review of the constitutional issue is urgently needed. This is even more true today because the Texas Supreme Court's denial of review has ripened the

split. As the amicus briefs submitted in this case demonstrate, taxing entities across the country are seeking guidance from the Court on this important issue.

II. The conflict is due to differing constitutional analyses, not to the application of the same legal test to materially different facts.

The Texas and Oklahoma courts reached opposite results in answering the same constitutional question. Peoples argues that this conflict is not worthy of this Court's review because "[t]he different results did not stem from disagreement over the federal constitutional test; the courts resolved different factual circumstances relating to different pipelines." Br. Opp., at 2. Peoples is wrong.

A. There are no material factual distinctions.

The facts underlying the two cases are identical in all important respects. Both cases involve attempts by local governmental authorities to impose an ad valorem tax on natural gas held in underground storage on a FERC-regulated interstate pipeline system. The Oklahoma court held that the gas is taxable under the dormant Commerce Clause, while the Texas court held that it is not. Peoples' attempt to

attribute these different results to mere factual distinctions misses the mark. Br. Opp., at 17.

An ad valorem tax is a tax on *property* based on its *value*. For state authorities to impose an ad valorem tax on the working gas held in a storage facility on January 1 of a given year, the material questions are: What volume of gas in the facility is allocable to each storage customer? And what is the value of each customer's allocable share?

The "factual distinctions" that Peoples identifies are either immaterial or non-existent. The first prong of the test of *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 279 (1977), is whether a tax "is applied to *an activity*" – not a taxpayer – "with a substantial nexus to the taxing State" (emphasis added). *See also* U.S. Br. (No. 08-1458), at 12 (as applied to a property tax, "the first prong of the *Complete Auto* inquiry" is "whether the *relevant goods* have a constitutionally sufficient nexus to the taxing State") (emphasis added). Under that analysis, it does not matter whether the taxpayer "intended" for its gas to be stored in a particular State, Br. Opp., at 17; it matters only that the taxpayer's gas *is* stored in that State. Nor does it matter whether the allocation of storage volumes for tax purposes is accomplished through a FERC-approved tariff establishing an apportionment formula, *id.*, or through a detailed analysis by the very pipeline company in charge of storing the gas. And it makes no difference whether the gas being taxed *originated* in the taxing State, *id.*;

it matters only that the customer's gas is *stored* in the taxing State. After all, it is the *storage* of the gas, regardless of its point of *origin*, that confers benefit on the shipper by permitting it to engage in price arbitrage, and that imposes burdens on local governmental authorities by requiring them to provide, among other things, roads, police, and fire protection.

Finally, the notion that the Oklahoma and Texas decisions are somehow materially different with respect to the issue of "ownership" is incorrect. Br. Opp., at 17. The Texas court employed the same basic reasoning as the Oklahoma court in rejecting Peoples' lack-of-ownership argument. *Compare* Pet. App., at 5-9 (concluding that, "for tax purposes, Peoples owns an allocation of the natural gas stored in Harrison County") *with In re Assessment of Personal Property Taxes Against Missouri Gas Energy*, 234 P.3d 938, 950-52 (Okla. 2008), *cert. denied*, 130 S. Ct. 1685 (2010).

In sum, the direct conflict between the Oklahoma and Texas decisions cannot be attributed to purported factual distinctions. The conflict is due solely to the courts' differing constitutional analyses, which is why review and clarification by this Court is urgently needed.

B. Review is needed to clarify the role, if any, of the older "continuity of transit" cases.

As the Solicitor General observed, this Court has yet to decide "whether or to what extent *Complete Auto* displaces the older line of 'continuity of transit' cases in the specific context of state ad valorem taxes on goods temporarily held in storage during the course of interstate transport." U.S. Br. (No. 08-1458), at 10. The conflicting decisions illustrate the consequences of that continuing uncertainty. The Oklahoma court concluded that the older "continuity of transit" cases were "superseded" by this Court's decision in *Complete Auto*. *Missouri Gas*, 234 P.3d, at 959 n.84. The Texas court, in contrast, found the older "in transit" analysis to be "crucial" to the Commerce Clause inquiry. Pet. App., at 13.

Peoples argues that the "in transit" cases did not color the Texas court's "substantial nexus" analysis under *Complete Auto*. Br. Opp., at 15-16. Peoples is wrong. After a protracted discussion of the "in transit" cases, Pet. App., at 11-17, the Texas court emphasized Peoples' interstate activities of "engag[ing] in the purchase and delivery of natural gas to its customers in Chicago," *id.* at 20. The court dismissed "the generic act of storing gas in a reservoir in Harrison County," *id.*, at 19-20, which should have been dispositive of the "substantial nexus" inquiry in this case involving an ad valorem tax on *property*.

In contrast, the Oklahoma court did not rely on the "continuity of transit" analysis in applying *Complete Auto*, and it criticized the Texas court for having done so. *Missouri Gas*, 234 P.3d at 959 n.84. The Oklahoma court did not misread the Texas court's opinion. The court read the opinion correctly and disagreed with it, setting up a clear split that this Court should resolve.

By misapplying the "continuity of transit" analysis to the *Complete Auto* test, the Texas court caused *intrastate* and *interstate* storage gas to be treated differently. Thus, storage gas that is taxable in Oklahoma is not taxable in Texas because of conflicting interpretations of federal constitutional law. And appraisal districts in Texas are compelled to segregate intrastate storage gas (which is taxable) from interstate storage gas (which is not), even though both classes of storage customers benefit equally from the storage. CCAD Amicus Br., at 11. The principles of federalism that undergird dormant Commerce Clause analysis were intended to prevent discrimination against interstate commerce. *Complete Auto Transit*, 430 U.S. at 279. They were not intended to favor interstate over intrastate commerce. *Id.* at 288 (citing *Western Live Stock v. Bureau of Revenue*, 303 U.S. 250, 254 (1938), and *Colonial Pipeline Co. v. Traigle*, 421 U.S. 100, 108 (1975)). But the latter is the result of the Texas court's decision. Worse, without guidance from this Court, cash-strapped taxing authorities in other states (except for Oklahoma)

will be compelled either to follow the Texas decision and forgo much-needed revenue, or to follow the Oklahoma decision and face inevitable litigation with one of the largest industries in the country.

C. Review is needed to clarify the role, if any, of the *Quill* "physical-presence" rule.

Review is also needed to decide whether or in what manner the *Quill* "physical-presence" rule applies to Commerce Clause scrutiny of a state property tax. *See Quill Corp. v. North Dakota*, 504 U.S. 298, 312-14 (1992). Peoples argues that there is not "any conflict over the 'physical presence' test." Br. Opp., at 1. But Peoples is wrong.

The Texas court cited *Quill* in support of its erroneous conclusion that it is the *taxpayer's* physical presence and activities in the State, not the *property's* physical presence, that matter. *See* Pet. App., at 19 ("The Commerce Clause requirement of a substantial nexus with the taxing state is satisfied by the taxpayer's physical presence in the state.") (citing *Quill*, 504 U.S. at 312-14, and two state cases). Contrary to Peoples' attempt to recast the Texas court's reasoning, that Court did not cite *Quill* merely to note that physical presence of the taxpayer was sufficient, but not necessary, to satisfy the "substantial nexus" element of *Complete Auto*. It is clear from the face of the opinion that, to pass dormant Commerce Clause

scrutiny, the Texas court would require the taxpayer's physical presence and activity in the state even when a property tax is at issue.

The Texas court virtually ignored the massive presence of Peoples' storage gas in Harrison County. It focused instead on *Peoples'* lack of a physical presence, emphasizing that Peoples has no office, employees, representatives, or physical facilities in the State. Pet. App., at 19. The court also emphasized that it was Pipeline, not Peoples, that directed where the gas was to be stored, concluding that "we are to consider not whether Pipeline's activities have a substantial nexus with the State, but whether Peoples' activities do." *Id.*

The Oklahoma court took a completely different approach. It expressly criticized the Texas court for its focus on Peoples' activities and its *in personam* type of contacts with the taxing jurisdiction, rather than on the property actually being taxed:

> We are convinced that the Texas court's focus on the parties' activities and their *in personam* types of contacts with the taxing state is mistaken. The tax at issue is an ad valorem property tax, a tax on property where it is located, not on the taxpayer's activities.

Missouri Gas, 234 P.3d at 959 n.84. Again, the Oklahoma court did not misread the Texas court's opinion.

The courts applied differing constitutional tests, and that conflict explains the courts' different responses to the same constitutional question.

Neutral observers agree. Professor Hellerstein noted the conflict and, like the Oklahoma court, concluded that the Texas court erred by misplacing its focus on the *taxpayer's* physical presence in the taxing jurisdiction rather than on the *property's* presence. 1 J. Hellerstein & W. Hellerstein, State Taxation ¶ 4.13[3][a] (3d ed. 2010).

Thus, there is a very real conflict regarding the proper role of "physical presence" in the context of modern dormant Commerce Clause scrutiny of a state property tax. Review by this Court is needed to resolve it.

III. "Unresolved" state-law grounds should not deter this Court's review.

Peoples argues that this Court should decline review because state law grounds *might* provide an independent ground for affirmance. Br. Opp., at 19. That is no obstacle to this Court's review.

Peoples' argument is not a jurisdictional one. Nor could it be. The Texas opinion "fairly appears to" (indeed, indisputably does) "rest primarily on federal law" and lacks the requisite "plain statement" (or any statement) to the contrary. *Florida v. Powell*, ___ U.S. ___, 130 S. Ct. 1195, 1201, 1203 (2010) (citing

Michigan v. Long, 463 U.S. 1032, 1040-42 (1983)). Far from "underl[ying] proper consideration of the nexus issue," Br. Opp., at 20, Peoples' three state-law arguments were either expressly rejected by the court below (ownership) or left unreached (allocation and state tax statute) because of the decision on the dispositive Commerce Clause issue.

At most, these state-law arguments are potential alternative grounds by which the state court might reach the same result on remand. Setting aside that none of the state-law arguments has merit, as petitioner is prepared to demonstrate on remand, the mere existence of potential state-law issues on remand would not make this Court's decision on the Commerce Clause issue "advisory." Br. Opp., at 21. Indeed, the state court would be "freer" to consider the state-law issues on remand "because it is disabused of its erroneous view of what the United States Constitution requires." *Arizona v. Evans*, 514 U.S. 1, 8 (1995).

It is not unusual for this Court to decide federal-law issues despite potential alternative state-law grounds for reaching the same result on remand. *See, e.g., Pennhurst State Sch. and Hosp. v. Halderman*, 451 U.S. 1, 9, 30-31 (1981) (reversing decision that federal statute mandated treatment of the mentally retarded in the least restrictive setting and remanding claim that Pennsylvania statute contained similar requirement). The court below chose to resolve this case on federal constitutional grounds, the Texas

Supreme Court chose to leave that decision undisturbed, and this Court is the "final arbiter[ ] of important issues under the federal constitution." *Arizona v. Evans*, 514 U.S. at 9 (quoting *Minnesota v. Nat'l Tea Co.*, 309 U.S. 551, 557 (1940)).

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Harrison Central Appraisal District,
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Respondent

On Petition for Writ of Certiorari to the Texas Court of Appeals, Sixth Appellate District

BRIEF OF CHAMBERS COUNTY APPRAISAL DISTRICT, LIBERTY COUNTY CENTRAL APPRAISAL DISTRICT, SMITH COUNTY APPRAISAL DISTRICT, AND THE TEXAS ASSOCIATION OF APPRAISAL DISTRICTS AS *AMICI CURIAE* IN SUPPORT OF PETITIONER

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U.S. ENERGY INFORMATION ADMINISTRATION, *Top Natural Gas Producing States*, 2007, http://www.eia.doe.gov/neic/experts/natgastop10.htm 6, 7

U.S. ENERGY INFORMATION ADMINISTRATION, *State Energy Profiles: Texas*, http://www.eia.doe.gov/state/state_energy_profiles.cfm?sid=TX.....6

U.S. ENERGY INFORMATION ADMINISTRATION, *Underground Natural Gas Storage Capacity Summary*, 2009, EPG0_SAC_Mmcf_a.htm.....7

Pursuant to Rule 37 of this Court, the Chambers County Appraisal District, the Liberty County Central Appraisal District, the Smith County Appraisal District of Texas and the Texas Association of Appraisal Districts (hereinafter "the Districts")[1] respectfully submit this brief in support of the Petitioner, the Harrison Central Appraisal District, for a writ of certiorari in the above-captioned matter.[2] The *amici curiae* urge that the Court grant the petition for a writ of certiorari and that the decision of the Texas Court of Appeals, Sixth Appellate District be reversed.

INTEREST OF THE *AMICI CURIAE*

Interstate pipelines operate natural gas storage fields throughout the United States.[3] At the end of 2008, there were over 217,000 miles of interstate pipelines in the United States and over 58,000 miles

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[1] In accordance with Rule 37 6, *amici* state that no counsel for a party has authored this brief, in whole or in part No person or entity, other than *amici curiae*, have made a monetary contribution to the preparation or submission of this brief.

[2] In accordance with Rule 37.2(a), *amici* state that the counsel of record for all parties received notice of their intention to file a brief in support of the Petitioner at least 10 days prior to the due date for the brief Written consent of the Petitioner and Respondent was obtained from their counsel of record

[3] U.S ENERGY INFORMATION ADMINISTRATION, *Interstate National Gas Supply Dependency*, 2007, http://www.eia.doe gov/pub/oil_gas/natural_gas/analysis_publications/ngpipeline/dependstates_map html (last visited Feb 8, 2011).

of pipeline in Texas.[4] Approximately, 1,772,335 jobs are supported by the natural gas and petroleum industries in Texas. These jobs add $293.8 billion to Texas' gross state product, or 24.2% of its wealth.[5] At the end of 2007, there were approximately 400 underground natural gas storage facilities in the United States. Many of these storage facilities were located in Texas.[6] There are other storage facilities in Texas that include stored products other than natural gas that are shipped in intrastate commerce, such as oil and manufactured goods. Therefore, the issue of appraising and taxing stored goods in interstate commerce is a significant concern for Texas property tax authorities.

Like the Petitioner, the Districts are all political subdivisions of the State of Texas. *See* TEX. TAX CODE ANN. § 6.01(c) (West, Westlaw through 2009 Reg. Legis. Sess.). Moreover, like the Petitioner, interstate pipelines operate and store natural gas with other petroleum and industrial products in the Districts' jurisdiction.

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[4] U.S ENERGY INFORMATION ADMINISTRATION, *Estimated Natural Gas Pipeline Mileage in the Lower 48 States, Close of 2008*, http://www.eia doe gov/pub/oil_gas/ natural_gas/ analysis_publications/ngpipeline/mileage html (last visited Feb 8, 2011).

[5] AMERICAN PETROLEUM INSTITUTE, http //www api.org/ policy/americatowork/upload/JOBS_TEXAS.pdf (last visited Feb 8, 2011).

[6] U S ENERGY INFORMATION ADMINISTRATION, *U S Underground Natural Gas Storage Facilities, Close of 2007*, http //www eia doe gov/pub/oil_gas/natural_gas/analysis_publications/ngpipeline/undrgrndstor_map html (last visited Feb 8, 2011)

The Chambers County Appraisal District, the Liberty County Central Appraisal District, the Smith County Appraisal District of Texas, the Texas Association of Appraisal Districts[7] and other appraisal districts in this country need clear guidance from this Court on what properties they can include on their property tax rolls The taxing units that the *amici* appraise for also are significantly impacted because they depend on property taxes on such properties to provide critical governmental services.

REASONS TO GRANT THE PETITION FOR WRIT OF CERTIORARI

Because the annual *ad valorem* appraisal and potential taxation of stored natural gas and other "stored" goods in interstate commerce present recurring issues for these Districts and the taxing units they appraise for in Texas (in addition to many others throughout the United States) the Court should grant the Petitioner's writ of certiorari.

By granting the petition for writ of certiorari in this case the Court would have the opportunity to: (1)

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[7] The Texas Association of Appraisal Districts, Inc. is a statewide, voluntary non-profit organization incorporated and organized to promote the effective and efficient functioning and administration of appraisal districts in Texas In 2010, more than 90 percent of the state's 254 appraisal districts belong to TAAD, as well as numerous tax officials from school districts, cities, counties, state agencies and other entities, and other property tax professionals TAAD, *About Us*, http //www taad.org/about_us html (last visited Feb. 8, 2011)

address the correct application of the four part "test" this Court set forth in *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274 (1977) to an *ad valorem* tax matter, which would be an issue of first impression; (2) address the impact of the *Complete Auto* case on this Court's precedents regarding the ability of State and local taxing units to assess *ad valorem* taxes on goods stored by a common carrier prior to the beginning of interstate transit in interstate commerce; (3) provide taxpayers as well as state and local taxing units needed guidance as what constitutes "substantial nexus" under the first prong of the *Complete Auto* Test; and (4) resolve the disagreement and confusion regarding the constitutional limitations on a local or state taxing entity's ability to impose an *ad valorem* tax on stored natural gas that currently exists between Texas and Oklahoma.

SUMMARY OF THE ARGUMENT

Imposition of an *ad valorem* tax on natural gas stored in the State pending transport via an interstate pipeline to out-of state owners does not violate the Commerce Clause of the U.S. Constitution. By granting the petition for writ of certiorari, this Court can confirm this conclusion and further its Commerce Clause jurisprudence, especially as it relates to *ad valorem* taxation. Ever mindful of the Court's admonition in Rule 37.1 to not burden it with repetitious arguments, we defer to the Petitioner, Harrison Central Appraisal District's brief on behalf of the *amici* for most arguments.

ARGUMENT

A. Overview

1. The Texas *Ad Valorem* Appraisal and Tax Structure.

Article VIII, section 1 of the Texas Constitution requires that all real and tangible personal property used for the production of income, unless exempt, be taxed "in proportion to its value, which shall be ascertained as may be provided by law." TEX. CONST. art. VIII, § 1(b); *see also* TEX. TAX CODE ANN. § 11.01 (West, Westlaw through 2009 Reg. Legis. Sess.). It also requires that taxation be "equal and uniform." TEX. CONST. art. VIII, § 1(a). The Texas Constitution further requires that "all lands and other property not rendered for taxation by the owner thereof shall be assessed at its fair value by the proper officer." TEX. CONST. art. VIII, § 11.

The Texas Tax Code codifies the constitutional obligation of our state government to appraise and assess property for purposes of taxation. *See Atascosa County v. Atascosa County Appraisal Dist.*, 990 S.W.2d 255, 257 (Tex. 1999). As a part of this codification, the Texas Legislature in the Tax Code created appraisal districts to begin operation January 1, 1982, as political subdivisions of the state. *See* TEX. TAX CODE ANN. § 6.01 (West, Westlaw through 2009 Reg. Legis. Sess.). This statute establishes an appraisal district in each county and makes the appraisal district responsible for appraising property in the district for *ad valorem* tax

purposes of each taxing unit that imposes *ad valorem* taxes on property in the district.

Consequently, the appraisal districts are the Texas entities that must determine the taxability of all real and personal property for all local governments that impose a property tax. The appraisal districts must make the determination as to whether a particular property is taxable or exempt. *See* TEX. TAX CODE ANN. § 11.45(a) (West, Westlaw through 2009 Reg. Legis. Sess.). Therefore, the appraisal districts must annually determine whether goods are exempted by operation of the Dormant Commerce Clause.

2. Underground Storage.

Natural gas is an abundant, colorless, odorless, gaseous hydrocarbon that supplies the United States with 23.4 percent of its energy.[8] Every day millions of cubic feet of natural gas are transported from producing states to markets in other states through interstate pipelines. In 2007, Texas, Oklahoma, New Mexico and Louisiana were four of the top five natural gas producing states.[9] Texas is the nation's

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[8] U S ENERGY INFORMATION ADMINISTRATION, *U.S. Primary Energy Flow By Source and Sector, 2009*, http: //www eia doe gov/aer/pecss_diagram html (last visited Feb 8, 2011), U.S ENERGY INFORMATION ADMINISTRATION, *Kids Glossary*, http //www.eia doe gov/kids/energy cfm?page= kids_glossary#N (last visited Feb 8, 2011)

[9] U S ENERGY INFORMATION ADMINISTRATION, *Top Natural Gas Producing States 2007*, http.//www eia doe gov/neic/experts/natgastop10 htm (last visited Feb 8, 2011)

largest producer of natural gas, accounting for three-tenths of total U.S. natural gas production.[10]

"Underground gas storage facilities are a necessary and integral part of the operation of piping gas from the area of production to the area of consumption." *Schneidewind v. ANR Pipeline Co.*, 485 U.S. 293, 295 n.1 (1988).

The U.S. Department of Energy's Energy Information Administration reports that at the close of 2007 there were 400 underground natural gas storage facilities in 30 states, with several in Texas.[11] In 2009, Texas' natural gas storage capacity was 766,768 billion cubic feet, placing it fourth in the nation behind Michigan, Illinois, and Pennsylvania.[12]

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[10] U.S. ENERGY INFORMATION ADMINISTRATION, *State Energy Profiles, Texas*, http://www.eia.doe.gov/state/state_energy_profiles.cfm?sid=TX (last visited Feb. 8, 2011); U.S. ENERGY INFORMATION ADMINISTRATION, *Top Natural Gas Producing States 2007*, http://www.eia.doe.gov/neic/experts/natgastop10.htm (last visited Feb. 8, 2011).

[11] U.S. ENERGY INFORMATION ADMINISTRATION, *U.S. Underground Natural Gas Storage Facilities, Close of 2007*, http://www.eia.doe.gov/pub/oil_gas/natural_gas/analysis_publications/ngpipeline/undrgrndstor_map.html (last visited Feb. 8, 2011).

[12] U.S. ENERGY INFORMATION ADMINISTRATION, *Underground Natural Gas Storage Capacity Summary, 2009*, http://www.eia.gov/dnav/ng/ng_stor_cap_a_EPG0_SAC_Mmcf_a.htm (last visited Feb. 8, 2011).

Underground product is typically stored in three types of facilities: (1) depleted reservoirs in oil and/or gas fields; (2) aquifers; and (3) salt cavern formations. Two of the most important characteristics of an underground storage reservoir are: (1) its capacity to hold product for future use; and (2) the rate at which product inventory can be withdrawn—its deliverability rate.

Natural gas in the United States is typically stored in depleted natural gas or oil fields that are close to consumption centers. Conversion of a field from production to storage duty takes advantage of existing wells, gathering systems, and pipeline connections. Depleted oil and gas reservoirs are the most commonly used underground storage sites because of their wide availability.[13]

Aquifers are suitable for gas storage if the water bearing sedimentary rock formation is overlaid with an impermeable cap rock. While the geology of aquifers is similar to depleted production fields, their use in gas storage usually requires more base (cushion) gas and greater monitoring of withdrawal and injection performance. Deliverability rates may be enhanced by the presence of an active water drive. Most aquifers that are now converted gas storage reservoirs are located in the Midwestern United States.[14]

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[13] NATURALGAS.ORG, *Storage of Natural Gas*, http //www naturalgas org/naturalgas/storage.asp (last visited Feb 8, 2011)

[14] *Id*

Salt caverns provide very high withdrawal and injection rates relative to their working gas capacity. Base gas requirements are relatively low. Salt cavern construction is more costly than depleted field conversions when measured on the basis of dollars per thousand cubic feet of working gas capacity. However, the ability to perform several withdrawal and injection cycles each year reduces the per-unit cost of each thousand cubic feet of gas injected and withdrawn.[15] The majority of salt cavern storage facilities are in Texas, and in a few Gulf Coast states, such as Louisiana and Mississippi.[16]

The principal owners/operators of underground storage facilities are interstate pipeline companies. If a storage facility serves interstate commerce, it is subject to the jurisdiction of the Federal Energy Regulatory Commission (FERC).

Owners/operators of storage facilities are not necessarily the owners of the product held in storage. Indeed, most working product held in storage facilities is held under lease with shippers or end users who own the gas.

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[15] *Id*

[16] U.S. ENERGY INFORMATION ADMINISTRATION, *U.S. Underground Natural Gas Storage Facilities, Close of 2007*, http://www.eia.doe.gov/pub/oil_gas/natural_gas/analysis_publications/ngpipeline/undrgrndstor_map.html (last visited Feb. 8, 2011).

3. This Issue Has A Substantial Impact on *Amici*.

According to Capital Appraisal Group, which is the independent appraisal company hired by Chambers CAD to list and appraise the storage caverns and inventory contained therein for *ad valorem* tax purposes,[17] one of the largest underground salt dome storage terminals for natural gas liquids in North America is in Chambers County, Texas. These facilities located in Chambers County are actually 31 individual caverns, interconnected by piping. The inventory can be up to 18 different types of products, such as propane, ethane, butane or diesel. However, the facility is also used to store natural gas. These underground caverns contain a total storage capacity of 355,740,000 barrels of product according to the Texas Railroad Commission H10-H reports. These domes are located under the City of Mont Belvieu, Texas. The 31 caverns have 117 injection wells for insertion and removal of stored product. There are six owners of the caverns.

Normally those caverns may only operate at 17 or 18% of their total capacity. In dollar terms, for the recent tax years in 2008, $1,318,252,170 was the taxable value, with $146,964,020 exempted, in 2009, $919,095,870 in value was taxed, $136,161,120 was exempted and in 2010, $901,638,200 was taxed, $361,143,150 was exempted. The amounts exempted were based upon this Court's prior rulings

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[17] TEX. TAX CODE ANN. § 25 01(b) (West, Westlaw through 2009 Reg Legis Sess)

prohibiting taxation of property in the hands of a common carrier for interstate shipment. The taxing authority attempted to include only product in storage for this purpose.

The Chambers County salt domes are connected to eleven Federal Energy Regulatory Commission regulated pipelines and numerous intrastate pipelines, which transport product to out of state purchasers, in-state purchasers, and, in some cases, back to in-state refineries (some of the stored product is used as refinery feedstock). The principal gas pipeline is an interstate pipeline that travels through East Texas into other states, with branches to Florida, Eastern Tennessee and Pennsylvania. This facility is a veritable cluster of caverns and pipelines. A map of the facility resembles a spider's web of pipelines. The economic relationships among the storage facility owners, stored product owners, ultimate customers, and pipeline owners are vastly more complex.

Perhaps most important for the Court's consideration is that the benefits and protections afforded to the owners of taxable, intrastate bound product and exempt interstate bound product are identical. The product of one owner, stored in a portion of the same facility, will be taxed because it has an in-state destination, while the product of another will be exempt because it has an out-of-state destination and is in a storage cavern owned by and connected to an interstate common carrier pipeline. In one case, a company owns two caverns, one connected to an interstate pipeline and the other

connected to an intrastate pipeline, with the two caverns connected to each other. That company can transfer the product between the two caverns to suit its business needs.

Of *amici*, the facts in Chambers County are most similar to the facts in the present case and in *In re Assessment of Personal Property Taxes Against Missouri Gas Energy*, 234 P.3d 938, 959 (Okla. 2008), *cert denied*, 130 S. Ct. 1685 (2010). Most, but not all, of the product stored is produced in Texas refining facilities or chemical plants. Other storage facilities are utilized for natural gas. Those products that are bound for out-of-state delivery are in the hands of the common carrier pipeline. The interstate journey for most begins at the facility. Much of the product has been purchased for out-of-state delivery while awaiting shipment at the storage facility, just as was the case in Oklahoma. *Id.* at 943. The seminal issue regarding most of the stored products in Chambers County is when the interstate journey begins. The interstate pipelines mostly begin at this location. However, as with other facilities, some stored product at this location may have been delivered from refineries or gas fields in other states or foreign nations, thus prompting the need to determine whether interstate transit has been interrupted by the owner's business needs or by storage necessary for interstate transit.

Smith County Appraisal District appraises for all the taxing entities within Smith County, Texas. It is also located near Harrison County, Texas. Smith CAD has several oil tank farms within its

jurisdiction. The market value of the oil in tanks in Smith County is over $65,000,000.

Liberty County Central Appraisal District also possesses salt domes with working gas capacity in the billions of cubic feet in its jurisdiction. Liberty County's salt domes are proximate to interstate and intrastate pipelines, along other facilities. There is currently $443,321,400 worth of inventory contained in storage caverns within Liberty County, Texas.

Also within the Liberty County Appraisal District is a rail yard, where millions of dollars worth of product sits in railcars at any given time. The product is sent there to wait for orders from customers. Once the order is received the car is sent out. However, like the storage cavern in this case, the rail yard is used to store product for the convenience and business purpose of the owner until the owner needs the product. For the 2010 Tax Year, there was $276,418,970 worth of taxable product sitting in the rail yard on January 1. That amount of value represents 43% of the appraisal roll of the City of Dayton, Texas.

B. This Matter Gives The Court An Opportunity to Further Address the Commerce Clause, Especially In Regards To *Ad Valorem* Taxation.

In *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274 (1977), this Court overruled a line of decisions which established a *per se* bar to the taxation of property in interstate commerce. In doing so, it

adopted a four-prong test for deciding whether a particular state tax survives Commerce Clause scrutiny. A state tax will be sustained if it: (1) is applied to an activity with a substantial nexus to the taxing State; (2) is fairly apportioned; (3) does not discriminate against interstate commerce; and (4) is fairly related to the services provided by the State. *Id.* at 279.

Ad valorem taxes are assessed by state and local governments across the United States. *Ad valorem* taxes are one of the primary pillars supporting the services state and local governments provide. By granting certiorari and addressing the issues in this case, the Court, in a matter if first impression, could address the *Complete Auto* Test as it relates to *ad valorem* taxes on goods in interstate transit on massive amounts of goods constantly present in a jurisdiction, in interstate commerce.

Presently most of the property tax issues concerning taxation of interstate commerce are issues related to the taxation of goods stored incident to interstate and intrastate transit. Most issues involving the instrumentalities of commerce have been resolved utilizing *Complete Auto* standards. The law concerning taxation of goods stored incident to interstate and intrastate commerce, however, is governed by rules which substantially predate the *Complete Auto* decision. Those rules were developed in eras where commerce was substantially slower and simpler. They involve taxation of lumber being transported by river (*Coe v. Town of Errol*, 116 U.S. 517, (1886), *Hughes Bros. Timber v State of Minn.*,

272 U.S. 469 (1926)); cattle in stockyards (*Minn. v. Blasius*, 290 U.S. 1 (1933)); sheep pasturing while traveling through a state (*Kelley v. Rhoads*, 188 U.S. 1 (1903)); and oil segregated in barrels for shipping (*General Oil v. Crain*, 209 U.S. 211 (1908)).

Essentially, these cases were developed in the late 19th and early 20th centuries in the context of a Court imposed prohibition upon the taxation of interstate commerce that existed until *Complete Auto*. The rules turn on determining when the transit physically or constructively begins. Once the transit has begun and is interrupted by storage, a fine-line must be drawn between whether the storage was necessarily incident to the goods' interstate transit or for the owner's business reasons.

After *Complete Auto* where the Court removed the blanket prohibition on the taxation of interstate commerce and replaced it with a modern analysis that seeks to prevent taxation from becoming an undue burden on interstate commerce, the pre-*Complete Auto* rules on taxation of goods in transit are anachronistic and difficult to administer in the modern world of complex commerce.

At least one treatise has characterized this Court's opinions in this field as being not very helpful when determining when a state may tax during an interruption to an interstate journey. Paul Hartman, *Federal Limitations on State and Local Taxation* 383 (1981). Equal difficulties arise in determining when interstate commerce begins.

Texas taxing authorities have struggled with the difficulty of applying this Court's pre-*Complete Auto* rules to the taxation of goods in commerce. As Texas authorities understand these rules, interstate journey begins when the property movement has begun or when the property is delivered to a common carrier for shipment. *See Coe v. Town of Errol*, 116 U.S. 517 (1886); *Marathon Ashland Petroleum L.L.C. v. Galveston Cent. Appraisal Dist.*, 236 S.W. 3d 335 (Tex. App.—Houston [1st Dist.] 2007, no pet.) In *Marathon Ashland* for example, the issue of taxability turned on the fact that the owner stored the product in its own facilities, which were connected to the interstate pipeline by a valve. Id. at 336. In *Virginia Indonesia Co., v. Harris County Appraisal District*, 910 S.W.2d 905, 912-13 (Tex. 1995), *cert. denied*, 518 U.S. 1004 (1996), the Texas Supreme Court, while addressing an export issue, expressly stated that until the United States Supreme Court overruled *Coe v. Town of Errol*, the court would continue to apply the doctrines to Texas cases.[18]

In Chambers County, the common carrier pipelines own many of the storage caverns, in which they constantly store refined product or natural gas incident to interstate shipment, after taking delivery of the product. The product is often sold while awaiting interstate shipment. There is a constant presence of stored product at this location. Similar

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[18] Following this Court's statement in *Rodriguez de Quijas v. Shearson/Am Express, Inc*, 490 U S. 477, 484, (1989)

situations exist across the state's vast petrochemical industry.

As briefly noted above and as documented in the facts applicable in the companion case, locally gathered product is often intermingled with imported product in the same storage facility. *See Midland Cent. Appraisal Dist. v. BP Am. Prod. Co.*, 282 S.W.3d 215, 219 (Tex. App. – Eastland 2010 pet. denied), *seeking cert.* cause no. 10-890. All the molecules are the same. This makes application of the Court's distinction between temporary storage for the owner's business reasons and storage incident to interstate transit extremely difficult.

When trying to apply the Court's standard of whether property is in the hands of a common carrier, current federal agency documentation regarding the destination of products held by a common carrier and destined for interstate transit is profoundly unhelpful. When the issue turns on whether a valve has been turned or even exists, the taxing authorities may not possess sufficient technical expertise to make the distinctions required by the Court's historical approach. The Court has never considered such documentation to be determinative, but tax administrators must rely on such information to make the threshold determinations of the product's status in transit.

Also, federal regulations make these determinations even more difficult. Property owners have relied upon Federal Energy Regulatory Commission rules to evade taxation. For example, property owners in

Texas have claimed that storage prior to shipment places the product in the protected interstate commerce stream, relying upon 18 C.F.R. § 284.1. This regulation simply defines transportation to include storage, exchange, backhaul, displacement, or other methods of transportation and was intended as a part of a process to prohibit discrimination in the shipping of natural gas. Nonetheless, it was a subject in the dissent in the Oklahoma Supreme Court's case on the same matter. *See In re Assessment of Pers. Prop. Taxes Against Mo. Gas Energy*, 234 P.3d at 956-7. The problem that these issues illustrate is that the reliance on pre-*Complete Auto* formulaic standards do not reflect the necessary policy considerations in determining whether a state or local tax should be considered an undue burden on interstate commerce.

Complete Auto brought this area of jurisprudence closer to the original meaning of the Commerce Clause. The standards announced in that decision should similarly be applicable to goods in interstate transit. *Amici* respectfully request that the Court grant petition for a writ of certiorari and provide a modern framework to address the issues that arise in the taxation of goods in interstate transit.

C. This Matter Gives the Court An Opportunity to Clarify Whether the Applicability of the Physical Presence Test To *Ad Valorem* Taxes and Further Explore What Constitutes "Substantial Nexus."

The Commerce Clause of the United States Constitution reserves to the Congress the power "to regulate commerce.., among the several states." U.S. Const., art. I, § 8, cl. 3. This Court has previously recognized a "negative" or "dormant" Commerce Clause power that "prohibits state taxation or regulation that discriminates against or unduly burdens interstate commerce and thereby, "imped[es] free private trade in the national marketplace." *Reeves, Inc. v. Stake*, 447 U.S. 429, 437 (1980).

Congress can act regarding interstate commerce, such as in the case of Public Law 86-262, 15 U.S.C. § 381, and the Mobil Telecommunications Tax Sourcing Act (MTSA), 4 U.S.C. § § 116-126, but unless and until it does so, state and local governments are faced with the distinct possibility that their exercise of taxing authority will impair interstate commerce. Therefore, they must err on the side of caution and not exercise that authority. If a state or local government does not hold back on the exercise of its authority, it risks violating the Constitution by trespassing on and narrowing congressional constitutional authority. The avoidance of that violation of congressional

authority is the foundation of all substantial nexus analysis.[19]

However, over the past quarter-century, nexus standards have been blurred for several reasons: (1) this Court has moved on from its historic holdings; (2) Congress has refused to act and clarify the issues involved; (3) state and local governments lack clear and commonly understood nexus standards and react in a number of various ways; and (4) when these state and local actions are taken to courts, inconsistent theoretical challenges to traditional physical presence nexus has manifested itself through a patchwork of recent cases. The cherry on this ice cream sundae of uncertainty regarding what constitutes constitutional nexus is the expanding pace and breadth of modern commercial transactions.

Based on the plain reading of this Court's jurisprudence, some sort of physical presence is

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[19] The courts, for sales and transactions taxes, have placed strict bounds on when a taxing authority may lawfully assert its authority over a remote taxpayer and that is only when the taxpayer has physical presence within that state. *See Quill v. N.D.*, 504 U.S. 298 (1992), citing *Gibbons v. Ogden*, 9 Wheat. 1, 231-232, 239 (1824). Only when a taxpayer is physically present in a state can that state exercise its taxing authority and compel an out-of-state taxpayer to collect and remit sales taxes on its behalf. Physical presence is created in various ways, including, but not limited to, offices, property, and employees located in a state. When those activities are direct, it can create substantial nexus and legally make a taxpayer subject to a state's taxing authority.

required to establish substantial nexus.[20] *Quill Corp. v. N.D.*, 504 U.S. 298 (1992); *Nat'l Bellas Hess v. Ill. Dep't of Revenue*, 386 U.S. 753 (1967). The "substantial nexus" prong of the *Complete Auto* Test is satisfied if there is "some definite link, some minimum connection between a state and the ... property ... it seeks to tax." *Allied-Signal, Inc. v. Dir., Div. of Taxation*, 504 U.S. 768, 777 (1992).

However, while the Court in *Quill* elaborated on, it did not reject all of, its prior dormant Commerce Clause analysis. Therefore, an unintended result is uncertainty of whether the physical presence requirements extend to taxes other than sales and use taxes. *Id.* at 314-317.

A leading tax commentator, has noted this uncertainty. Although "[s]ome of the results of the doctrinal changes" brought on by this Court in recent years "are clear,...the impact of the contemporary Commerce Clause philosophy on other cases decided in earlier eras, and the doctrine they spawned are less clear." 1 J. Hellerstein & W. Hellerstein, *State Taxation* para 4.13[1] (3d ed. 2010).

By granting the petition for writ of certiorari in this case, the Court could also clarify *Quill* and *Complete*

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[20] The Court in *Quill* noted the focus of the Commerce Clause and its substantial nexus requirements was not on fairness for individual defendants but on concerns of effects state regulation might have on the national economy *Quill*, 504 U S at 312

Auto's holdings for taxing units and taxpayers alike on the issue of whether temporarily stored goods "in transit" have a physical presence that subjects them to *ad valorem* taxation and whether such taxation contravenes the Commerce Clause. By granting the petition for writ of certiorari, this Court could also address whether the first prong of the *Complete Auto* Test is met under certain facts. In this case, there was a substantial amount of natural gas stored at all times in Harrison County, Texas throughout the year. Peoples owned part of the natural gas with a physical presence in Harrison County. The Court could resolve whether such property constituted a "definite link" and more than "some minimum connection" between Peoples' gas and Harrison County. In doing so, it would further the "substantial nexus" jurisprudence of this Court.

D. By Granting the Petition and Deciding This Case the Court Would Resolve the Disagreement Between Texas and Oklahoma, Equalizing the Demand on Government Services.

This Court should grant the petition for writ of certiorari to resolve the disagreements between Texas and Oklahoma's courts on the same constitutional question. Texas courts in this matter and one regarding Midland Central Appraisal District, have determined that the Commerce Clause *prohibits* state *ad valorem* taxation of constantly stored natural gas in an interstate pipeline system. *See Peoples Gas, Light and Coke Co. v Harrison Cent. Appraisal Dist.*, 270 S.W.3d 208 (Tex. App—

Texarkana 2008, pet. denied); *Midland Cent. Appraisal Dist. v. BP Am. Production Co.*, 282 S.W.3d 215 (Tex. App. —Eastland 2010 pet. denied). The Supreme Court of Oklahoma has held that the Commerce Clause *permits* such a tax. *See In re Assessment of Personal Prop. Taxes Against Mo. Gas Energy*, 234 P.3d 938, 959 (Okla. 2008), cert denied, 130 S. Ct. 1685 (2010). This conflict means natural gas on an interstate pipeline stored in Oklahoma is taxable but under the same facts is not in Texas. These rulings distort governmental services and the burdens paying for them.

The fourth prong of the *Complete Auto* Test requires the tax to be reasonably related to the extent of the contact. *Commonwealth Edison Co. v. Mont.*, 453 U.S. 609, 626 (1981).

A tax is a means of distributing the burden of the cost of government, not an assessment of benefits. *Id.* at 622-23. The "relevant inquiry" is not "the amount of the tax o[r] the value of the benefits allegedly bestowed as measured by the costs the State incurs on account of the taxpayer's activities," but whether the tax is "reasonably related to the extent of the taxpayer's contact" with the taxing jurisdiction. *Id.* at 626. In other words, "has the State given anything for which it can ask in return" *Id.* at 625.

Such benefits and protections are not hypothetical. While this brief was drafted, the fractionators unit at the Texas Enterprise Products facility at the salt domes in Mont Belvieu, Chambers County, Texas

exploded, within a few miles of a school, bringing local fire and police units into play. The fractionators serve to separate gases for interstate commerce. [21]

If the current split between the Texas ruling in this case and the Oklahoma Supreme Court's stands, there will be a clear economic incentive for property owners to store their product in Texas, where it will not be taxed, instead of Oklahoma where it will be taxed.

As noted above and as an example, the storage facility in Chambers County could go from normally operating somewhere around 18% of capacity to storing a much greater quantity of product. As capacity grows, the potential for an emergency would logically increase. This point could be illustrated by imagining by which facility you would prefer your house to be located – an empty storage cavern or a storage cavern filled with more propane and thus more fire prone. Although the taxing units of Chambers County will receive no additional revenue, they will have to provide more police protection, fire protection, emergency services, and other

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[21] CNN, *Fire Burning at Texas Natural Gas Facility*, http //www.cnn.com/2011/US/02/08/texas plant.fire/ (last visited Feb. 8, 2011); HOUSTON CHRONICLE, *Plant Burns In Mont Belvieu Enterprise Products Operates Facility in Chambers Co*, http://www chron com/disp/story.mpl/metropolitan/ 418224 tml (last visited Feb 8, 2011); KHOU, *Multiple Explosions, Fire at Mont Belvieu Plant*, http //www khou com/news/ cnn/Explosions-fire-at-Mont-Belvieu-plant--115579109.html (last visited Feb. 8, 2011)

governmental services to protect the property of owners such as Peoples'.[22]

Texas's *ad valorem* tax is a general revenue tax imposed for the support of local governments. The tax in this case applies to the presence of Peoples' property in Harrison County, Texas as of the January 1 assessment date. It is taxed to the same extent as all other personal property in the county.[23] Peoples is therefore being asked to shoulder no more than its fair share for the support of government-provided services and the "advantages of a civilized society." *Japan Line, Ltd. v. County of Los Angeles*, 441 U.S. 434, 445 (1979).

By granting the petition for writ of certiorari in this case and making a ruling that resolves this current disagreement between the highest Courts in Texas and Oklahoma, this Court would also level the demand for government services and their burdens to taxpayers between the two states – demands and

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[22] Professor Hellerstein sees 'no basis for the conclusion that the taxpayer's gas does not receive 'police and fire protection . . . and the advantages of a civilized society.'" 1 J. Hellerstein & W. Hellerstein, *State Taxation* para. 4.13[3][a] (3d ed. 2010).

[23] Contrary to the opinion of the Texas Court of Appeals in this case, it is not a tax on any activity of a business owner. Furthermore, ownership, location, and taxability of business personal property are not contingent upon a property owner having a physical business location. Business personal property that is stored in Texas is taxable, regardless of whether it is stored in a location owned by the owner of the personal property, or stored in a leased warehouse. *See* Tex. TAX CODE ANN. § 32.07(a) (West, Westlaw through 2009 Reg. Legis. Sess.).

costs that are currently skewed against Texas and its citizens.

CONCLUSION

For the above reasons, *amici* respectfully request this Court grant Harrison Central Appraisal District's Petition for Writ of Certiorari and reverse the decision below.

Respectfully submitted,

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IN THE SUPREME COURT OF THE UNITED STATES

HARRISON CENTRAL APPRAISAL DISTRICT,
Petitioner,

v.

THE PEOPLES GAS, LIGHT AND COKE COMPANY,
Respondent.

On Petition for a Writ of Certiorari to the Supreme Court of the United States

BRIEF OF *AMICUS CURIAE* METROPOLITAN COUNCIL OF APPRAISAL DISTRICTS IN SUPPORT OF PETITIONERS

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On Petition for a Writ of Certiorari to the Supreme Court of the United States

BRIEF OF *AMICUS CURIAE* METROPOLITAN COUNCIL OF APPRAISAL DISTRICTS IN SUPPORT OF PETITIONERS

The Metropolitan Council of Appraisal Districts (MCAD) respectfully submits this brief in support of the Petitioner Harrison Central Appraisal District (HCAD).[1]

[1] No counsel for a party authored this brief in whole or in part, and no counsel or party made a monetary contribution intended to fund the preparation or submission of this brief. No person other than *amicus curiae*, its members, or its counsel made a monetary contribution to the preparation or submission of this brief

Counsel of record of all parties received notice at least ten (10) days prior to the due date of the *amicus curiae's* intention to file this brief and the parties have consented to the filing of this brief

STATEMENT OF INTEREST

The Metropolitan Council of Appraisal Districts (MCAD) is a council of thirty of the largest appraisal districts in the State of Texas. Members of the MCAD include the Tax Appraisal District of Bell County, the Bexar Appraisal District, the Brazoria County Appraisal District, the Brazos County Appraisal District, the Cameron Appraisal District, the Collin Central Appraisal District, the Dallas Central Appraisal District, the Denton Central Appraisal District, the Ector County Appraisal District, the El Paso County Appraisal District, the Ellis Appraisal District, the Fort Bend Central Appraisal District, the Galveston Central Appraisal District, the Grayson Central Appraisal District, the Gregg Appraisal District, the Harris County Appraisal District, the Hays Central Appraisal District, the Hidalgo County Appraisal District, the Jefferson County Appraisal District, the Central Appraisal District of Johnson County, the Lubbock Central Appraisal District, the McLennan County Appraisal District, the Midland Central Appraisal District, the Montgomery Central Appraisal District, the Nueces County Appraisal District, the Parker County Appraisal District, the Potter-Randall Appraisal District, the Smith County Appraisal District, the Tarrant Appraisal District, the Central Appraisal District of Taylor County, the Travis Central Appraisal District, the Waller County Appraisal District, the Webb County Appraisal District, the Wichita Appraisal District, and the Williamson Central Appraisal District.

The Metropolitan Council of Appraisal Districts is interested in providing a fair and equitable appraisal system for *ad valorem* taxation for the citizens of the State of Texas. The primary purpose of the association is to institute and maintain a method of exchanging and interchanging information among appraisal districts of the State of Texas whose population exceeds 100,000 and/or whose total real and business personal property accounts total greater than 100,000 parcels.

MCAD's members have a direct interest in this case. Many of the MCAD's members' districts contain properties that will be affected by the outcome of this decision and ask the court to clarify the Texas state court jurisprudence so that they can efficiently, fairly, and effectively appraise the property in their jurisdiction. The following is a list of members and districts that have properties within their jurisdiction that contain stored natural gas, the tax assessment of which will be directly affected by the outcome of this case. While the effect of this case on MCAD members is not all inclusive of the effect on taxing districts in Texas, the number of entities affected allows this Court to fully understand that this decision is critically important to taxation in Texas and thus is of national importance.

The outcome of this case will also have an effect on the taxation of personal property located within MCAD members' districts beyond just the natural gas storage industry. The Harris County Appraisal District, Fort Bend Central Appraisal District, Brazoria County Appraisal District, and the Waller County Appraisal District all have salt dome

storage facilities that are maintained on properties within their jurisdiction in a manner factually similar to the gas storage facilities at issue in the case. Smith County Appraisal District has salt dome storage facilities and also oil tank farms that are maintained on properties within its jurisdiction in a manner factually similar to the gas storage facilities at issue in the case. The approximate value of the oil stored in the tank farms in Smith County is $65,000,000. Fort Bend County has salt dome storage properties that are maintained and factually similar to the gas storage facilities at issue in the case. Waller County has salt dome storage properties that are maintained and factually similar to the gas storage facilities at issue in the case.

The Tarrant Appraisal District has a multitude of gas and oil pipelines located within its jurisdiction that this decision may affect such as, but not limited to, the Atmos Energy Mid/Tex Pipeline, ExxonMobil Pipeline, Sunoco Pipeline, Texas Midstream Gas Services, Western Production, and the XTO Energy pipeline.

STATEMENT OF THE CASE

The Metropolitan Council of Appraisal Districts (MCAD) adopts and incorporates herein the Statement of the Case, The Statement of Facts, the Statement of Jurisdiction and the Issue Presented set forth in the Petitioner's Petition for Writ of Certiorari.

SUMMARY OF THE ARGUMENT

This Honorable Court should grant the Petition for Writ of Certiorari and rule on the merits of this matter so that all Texas appraisal districts will have a clear and uniform method to properly and accurately appraise natural gas being stored within their jurisdictions.

ARGUMENT

1. CONFLICTING JURISPRUDENCE IN STATE COURTS CREATES CONFUSION FOR TAX ASSESSORS AND TAXPAYERS ALIKE AND MUST BE RESOLVED IN ORDER FOR TAXATION TO BE FAIR AND UNIFORM NATIONWIDE.

The *ad valorem* taxation of natural gas in federally regulated storage facilities within the interstate transportation system presents a recurring issue that merits this Court's attention. The issue of taxing natural gas that is stored in one state and then transported to other states is a matter of nationwide concern and the clarity of the jurisprudence related to the same is of particular importance to Texas appraisal districts and taxing authorities nationwide who are statutorily charged with the obligation of taxing all non-exempt property in their respective state.

As previously stated, at the end of 2007, Texas had more than 25 underground natural gas storage facilities located in the southeastern, central, north

central, northeast northern and western parts of Texas.

Furthermore, this issue is not unique to Texas. In fact, at the close of 2007, there were 400 underground natural gas storage facilities in thirty states. There are currently five schools of thought regarding the issue at bar that taxing authorities in all of these thirty states must attempt to interpret before choosing to tax gas maintained locally in underground natural gas storage facilities.

In Mississippi, the Mississippi Supreme Court found, seemingly in conflict with this case, that a sufficient nexus existed to support taxation, overruling a Commerce Clause challenge regarding petroleum products in tanks in Mississippi which arrived by state pipeline, stayed for less than five days, and were injected into other pipelines for distribution in and out of the state. *Mississippi State Tax Commission v. Murphy Oil USA, Inc.*, 933 So.2d 285 (Miss. 2006).

In Louisiana, the jurisprudence on issues similar to the instant case relies on the archaic, pre-*Complete Auto* law, and Louisiana courts have held that gas that had come to rest in Louisiana resulting in hydrocarbons in a holding facility was taxable in Louisiana. *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274 (1977), *United Gas Pipe Line Co. v. Whitman*, 390 So.2d 913 (La. Ct. App. 1980), *writ denied.*, 396 So.2d 928 (La. 1981) and *Miss. River. Transmission Co. v. Simonton*, 442 So.2d 764 (La. Ct. App. 1983), *writ denied*, 444 So.2d 1240 (La. 1984).

In Florida, the courts found that petroleum products which were brought from out of state were

subject to local ad valorem taxation under the Commerce Clause holding that nexus existed under the *Complete Auto* analysis notwithstanding that the goods were "in transit" in interstate commerce. *Havill v. Gurley*, 382 So.2d 109 (Fla. Dist. Ct. App. 1980).

The Kansas Supreme Court, on similar but not identical facts, held that non-Kansas companies' allocations of gas storage were exempt from local ad valorem taxation. *See In the Matter of the Appeal of the Director of Prop. Valuation*, 284 Kan. 592, 161 P.3d 755 (2007).

Because there is a multitude of underground natural gas storage facilities located in various locations and counties across Texas and nationwide, every appraisal district or nationwide taxing authority with a storage facility or the potential to have a facility constructed in the future within its jurisdiction has a vested interest in the outcome of this litigation.

Unless this Court rules on the merits of this case and clarifies or overturns the Texas state jurisprudence on the matter, which specifically conflicts with Oklahoma state jurisprudence and the Solicitor General's opinion on the same (which this Court declined to grant Certiorari to correct), there is a possibility that a multiplicity of additional litigation will be necessary to settle all the remaining factual issues that may distinguish each appraisal district's or taxpayer's specific factual scenario.

Further, a resolution of this issue on a federal level would greatly further judicial economy and prevent costly and prolonged litigation. For

example, if a taxpayer happens to have a brick and mortar building in the county where the storage facility resides, the appraisal district or the taxpayer may be forced to sue to determine if the substantial nexus test is met under those circumstances. There is no doubt that fewer lawsuits will be filed concerning the taxation of natural gas in Texas and other states if the Court grants the Petition for Writ of Certiorari and rules on the merits.

As a result of the Texas Supreme Court's decision to decline the Petition for Review of the Texarkana Court of Appeals, it can be argued that Texas appraisal districts are prohibited from taxing working gas that is stored in storage tanks in their districts while taxing authorities in Oklahoma faced with the prospect of taxing the exact same facility are required to tax the same. This uneven application of the law governing application of taxation of products in interstate commerce is not acceptable as a matter of public policy. These unacceptable consequences can only be remedied by this Court. The state by state consequences if this Writ is not granted are vast and expansive.

If the Texas and Oklahoma Supreme Courts' differing and contradictory holdings are allowed to stand, misguided but good faith attempts by both taxing authorities and taxpayers alike will be forthcoming with a possibility of twenty-five more state Supreme Court decisions forthcoming (assuming, probably incorrectly, that no more of these facilities have been constructed in additional states) since 1997.

The dichotomy in available approaches to local taxing authorities would mean that if the wrong

authority for taxation was used, the entity would be in violation of the U.S. Constitution and result in needless expenditures of costs and resources to pursue taxation or defend the failure to tax property that is subject to taxation. Thus, this Court should grant Petitioner's Writ of Certiorari, review this case, and provide guidance for the uniform imposition of taxes on this commodity moving in interstate commerce.

II. THERE ARE TWO CASES ON WHICH PETITIONS FOR WRIT HAVE BEEN FILED ON THESE RELATED ISSUES, THUS SHOWING HOW IMPORTANT THESE ISSUES ARE AND PROVIDING A UNIQUE OPPORTUNITY FOR THIS COURT TO CLARIFY JURISPRUDENCE ON THIS SUBJECT.

On the same day that Harrison Central Appraisal District filed the Petition for Writ of Certiorari in this matter, the Midland Central Appraisal District filed Petition for Writ of Certiorari in *Midland Central Appraisal District v. BP American Production Company et al.*, 282 S.W.3d 215 (Tex. App – Eastland 2009, Petition denied). The facts of these cases are similar in that they both deal with storage of oil or gas in holding tanks associated with pipelines from the same.

In the *Midland* case, the Texas Court of Appeals held that a generally applicable, non-discriminatory *ad valorem* tax on an inventory of oil violated the dormant Commerce Clause. The taxation issue in the *Midland* case is essentially the same as in the case at bar; however, the *Midland* case deals with oil inventory and the instant case

deals with stored gas. On facts substantially similar to the *Midland* case, the Oklahoma Supreme Court concluded that a generally applicable, non-discriminatory *ad valorem* tax on inventory was constitutional.

Having two related Petitions for Writ of Certiorari presents an opportunity for the Court to better clarify this rule than any single petition is likely to permit. By taking this set of petitions, the Court can draw any appropriate distinctions between oil "tank farms" like that in the *Midland* case and the gas storage facilities in the instant case. This Court should not pass up the best opportunity this Court will have to speak on these issues.

When this issue was brought to the attention of this Court in *In re Assessment of Personal Property Taxes Against Missouri Gas Energy*, 234 P.3d 938 (Okla. 2008), *cert. denied*, 130 S. Ct. 1685 (2010), this Court sought the input of the United States Solicitor General who agreed with the Oklahoma Supreme Court's Ruling.

The fact that two cases are pending before this Court at this time reiterates the importance of resolving the dichotomy of state Supreme Court opinions which can only be resolved by this Court granting the Petitions for Writ of Certiorari in both this case and in the *Midland Central Appraisal District v. BP American Production Company et al., 282 S.W.3d 215* (Tex. App – Eastland 2009, Petition denied) case.

III. MCAD AGREES WITH PETITIONER THAT THE TEXAS APPELLATE COURT'S DECISION IS ERRONEOUS.

MCAD adopts the totality of Petitioner's Petition for Writ of Certiorari herein in lieu of rebriefing the same issues. However, the MCAD specifically points out that it concurs that the Court of Appeals erred in three ways.

First, the Court of Appeals erred in using this Court's "Continuity of Transit" analysis to eclipse the *Complete Auto* Analysis. The correct approach for this Court to adopt is outlined fully by the Oklahoma Supreme Court in *Missouri Gas,* which held that Petitioner failed to establish the unconstitutionality of applying Oklahoma's *ad valorem* tax on personal property to stored natural gas. The Solicitor General agreed with this holding.

Second, the Court of Appeals erred in applying *Quill's* "Physical-Presence" rule to *ad valorem* property taxation because the *Quill* case is narrow and should be limited to sales and use taxes which are clearly and wholly distinguishable from the taxes at hand. *Quill Corp. v. North Dakota,* 540 U.S. 298 (1992).

Finally, the Court of Appeals simply applied the *Complete Auto* test to the facts at hand incorrectly and should have found that, under the facts presented, the *Complete Auto* Test is completely and wholly satisfied. It is clear that the tax in question is fairly apportioned, since it only applies to gas that is actually in the storage tanks in Harrison County at the assessment date of January 1. The gas cannot be in two places at once on

January 1 and thus cannot be subject to double taxation. Furthermore, the tax plainly does not discriminate against interstate commerce, as it applies to any and all inventories. The gas also has nexus with the state because the property is actually physically present in the State on the assessment date. This Court has found sufficient nexus by the nature of the presence of the property being taxed. *See Commonwealth Edison Co. v. Montana,* 453 U.S. 609 (1981). Finally, and most clearly, the tax in question is patently fairly related to the services provided by the state. It is clear that local law enforcement and other government services would be required if there was a natural or manmade disaster at the storage facilities and it is counterintuitive to argue otherwise.

This incorrect jurisprudence will have a haunting effect on taxation in Texas and perhaps nationwide. Specifically this case, as well as the *Midland* case, creates a dangerous principle that a state cannot impose property taxes without showing a nexus to some business activity. This mistake in and of itself will wreak havoc on the appraisal district which seeks to fairly and legally assess *ad valorem* taxes upon property in its jurisdiction. Secondly, these decisions make it almost impossible for an appraisal district to pass the *Complete Auto* test as modified by these rulings because under these decisions if a property is in commerce, then it lacks the nexus and thus fails the first prong of the test.

CONCLUSION

For the foregoing reasons, *Amicus Curiae* respectfully request that this Court grant the Petition for Writ of Certiorari in this action.

Respectfully submitted,

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HARRISON CENTRAL APPRAISAL DISTRICT,

Petitioner,

v.

THE PEOPLES GAS, LIGHT AND COKE COMPANY,

Respondent

On Petition For A Writ Of Certiorari To The Texas Court Of Appeals, Sixth Appellate District

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QUESTIONS PRESENTED

How does the "substantial nexus" prong of *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274 (1977), apply to tangible personal property involved in commerce that is assessed a non-discriminatory ad valorem property tax:

- Is nexus, as the court below held, evaluated based on older "continuity of transit" cases exempting goods in the flow of commerce from paying their own way?
- Does nexus, as the court below held, also require a taxing authority to prove *in personam* "activity" by the taxpayer beyond the presence of the taxable *res* in the taxing jurisdiction?

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INTEREST OF AMICUS CURIAE

The amicus Texas Association of School Boards Legal Assistance Fund is an association of public school districts that plays a role in litigation likely to have a broad impact on its member districts.[1]

Those school districts have a particularly acute interest in the federal constitutional questions raised in this petition because the Texas school-funding system – like many local government entities across the country – depends on a local ad valorem property-tax system. Uncertainty over how ad valorem taxes fit into the Commerce Clause framework makes it more difficult to shape the local tax policy that supports critical services.

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[1] No counsel for any party has authored this brief in whole or in part, nor has any entity other than the named amicus curiae made a monetary contribution to the preparation or submission of the brief. *See* Sup. Ct. R 37.5 Timely notice was given to all parties, and each gave written consent *See* Sup Ct R. 37.2(a).

SUMMARY OF THE ARGUMENT[2]

There is now a split between two key states in the energy industry, Oklahoma and Texas, about what constitutional test applies to measure the taxability of oil and gas reserves under local ad valorem taxes.

Last Term, the Court had before it a petition challenging Oklahoma's side of the split. The Court called for the views of the Solicitor General, who expressed the view that Oklahoma had the better side of the argument and that, in any event, the Texas courts had not yet spoken with finality. Now they have, and there is no reason to delay this Court's review. A split between sister states about the federal law governing goods in transit deserves attention.[3]

The court of appeals embraced a "continuity of transit" test dating from a time when this Court had held that interstate commerce was by its nature exempt from state taxes. That test does not shed light on the modern *Complete Auto* framework, and importing it into the nexus prong threatens significant

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[2] This amicus brief is being submitted in support of this petition and in support of *Midland Central Appraisal District v. BP America Production Co*, No 10-890, both of which raise the same constitutional issues When necessary for clarity, the present petition is referenced as the "*Harrison* case" in contrast to the "*Midland* case."

[3] Federal circuits generally do not hear challenges to state ad valorem taxes because of the Tax Injunction Act. 28 U.S.C. §1341

damage to ad valorem property tax rolls, shifting the burden onto domestic taxpayers and, in effect, discriminating against intrastate commerce.

Further, the court of appeals adopted a legally incorrect view of how nexus should be tested for ad valorem property taxes. The court held that substantial nexus under *Complete Auto* requires a showing of *in personam* ("activity") contacts by the taxpayer rather than contact with the taxable *res*.

These petitions frame the problem well, and their contrasting facts offer a good vehicle to test the rule. Until this Court resolves these foundational questions under *Complete Auto*, both industry and taxing authorities will be wandering in the fog of Nineteenth Century "continuity of transit" case law that ill fits the modern economy and results in sharply disparate treatment of different industries based on features unrelated to the constitutional principles underpinning the Commerce Clause.

ARGUMENT

I. There Is an Entrenched Split About How the *Complete Auto* Framework Applies To Goods in Transit, Including Gas and Oil.

A. A split between Texas and Oklahoma that affects energy has broad importance.

Texas and Oklahoma have split on a question of constitutional law that creates uncertainty for the energy industry and local governments alike. The affected states are central to the national energy industry both in geography and geology.[4]

As things stand, when oil or gas flows through pipelines that cross the Red River, it leaves one view of federal law (Texas' more expansive one that shields the goods from taxes) and encounters a polar opposite view of federal law (which permits nondiscriminatory local taxes).

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[4] In arguing for certiorari in *Missouri Gas*, the American Gas Association pointed to a helpful Department of Energy map showing the web of gas pipelines across the lower 48 states. *See* Amicus Brief of American Gas Association, *Missouri Gas v. Schmidt* (No 08-1458), at 17 & 3a (map) That map remains the most current on the Department's website *See* "Interstate Natural Gas Supply Dependency, 2007," http://www.eia.doe.gov/pub/oil_gas/natural_gas/analysis_publications/ngpipeline/dependstates_map.html (visited Feb 6, 2010). In addition to the network of interstate pipelines, it highlights 30 states that "are at least 85% dependent" on the network for natural gas from producing states such as Texas and Oklahoma. *Id.*

Consider, for example, the newly tapped Barnett Shale, which is centered just below the Red River on the Texas side of the border. Should any of this gas be sent to a storage facility north of the Red River, it can be taxed; on the south side of the Red River, it is given complete federal immunity from taxation.

The split also touches neighboring states on the interstate pipeline system.[5] For example, Louisiana courts continue to apply the older "continuity of transit" analysis when determining whether goods can be assessed an ad valorem tax.[6] Formally, they apply state enactments made when "in transit" was prevailing federal law.[7] But with the present split of authority and without guidance from this Court, Louisiana policymakers do not know what latitude they have to loosen those restrictions over local ad valorem taxation.

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[5] For one example of how pipelines cut across these neighboring states, look at the pipeline in *Missouri Gas*. One of its two branches begins in Texas and runs through Oklahoma to Kansas, where it has a storage facility before reaching its endpoint. *Missouri Gas*, 234 P3d at 944. The other begins in Oklahoma, where it has a storage facility, and then merges together with the endpoint in Kansas *Id.*

[6] *E.g.*, *Mississippi River Transmission Corp v. Simonton*, 442 So 2d 764, 770 (La. Ct. App 1983).

[7] *Id.* at 770.

B. The split is firm and will not resolve itself.

The petitions now before the Court attack two Texas decisions that, serendipitously, came down as bookends around the Oklahoma Supreme Court's decision in *Missouri Gas*, one before and one after. Both states were aware of the split and further entrenched their conflicting positions.

The Oklahoma court noted the first Texas decision in conflict with its holding. *In re Assessment of Personal Prop. Taxes Against Mo. Gas Energy*, 234 P.2d 938, 959-60 (Okla. 2008). And it expressed its disagreement in no uncertain terms:

> [W]e remain unpersuaded by that court's reasoning. The Texas court first scrutinizes Harrison County's ad valorem tax using the traditional continuity of transit analysis, **a test we reject today as having been superseded** by the Supreme Court's decision in *Complete Auto Transit v. Brady*. . . .
>
> In addition, **we decline to follow the Texas court's reasoning** in concluding that the ad valorem taxation of storage of gas fails to meet the first and fourth prongs of the *Brady* test. . . .
>
> We are convinced that **the Texas court's focus on the parties' activities and their *in personam* types of contacts with the taxing state is mistaken.** The tax at issue is an ad valorem property tax, a tax on

> property where it is located, not on the taxpayer's activities.

Id. at 959-60 n.84 (emphasis added) (discussing *Harrison Cent. Appraisal Dist. v. Peoples Gas, Light & Coke Co.*, 270 S.W.3d 208 (Tex. App. – Texarkana 2008, pet. denied)). With only one justice dissenting, Oklahoma's position is firm.

Nor has Texas budged. At the time of the Oklahoma decision, the *Harrison* opinion it so harshly criticized was pending rehearing in the court of appeals. After supplemental briefing by both sides, that court left intact its opinion, cementing the split.[8]

And when the *Midland* opinion was issued, it even more explicitly rejected the core holding of the Oklahoma case – that the old "in transit" line of cases had been superseded by *Complete Auto*. Instead, it rested its decision on that very quicksand – reliance on the old continuity of transit analysis and looking for *in personam* contacts to support an ad valorem property tax.[9] *Midland Cent. Appraisal Dist. v. BP*

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[8] The *Harrison* opinion was issued on September 24, 2008 The Oklahoma opinion was issued on October 21, 2008 A letter brief was filed with the *Harrison* court on November 3, 2008, and a response was filed a few weeks later. The *Harrison* court denied rehearing on December 9, 2008. (Docket information for this case is available at the court website, http://www 6thcoa courts state tx us, using the "Case Search" feature and the docket number "06-07-00103-CV".)

[9] Indeed, when the *Midland* court sought to distinguish the facts from the Oklahoma case, it invoked the "in transit" reasoning that the Oklahoma court had rejected. *Midland*, 282 S.W.3d

(Continued on following page)

Am. Prod. Co., 282 S.W.3d 215, 221-23 (Tex. App. – Eastland, pet. denied) (analyzing continuity of transit); *id.* at 223-24 (using "in transit" to substitute for a nexus analysis); *id.* at 224 (looking for *in personam* contacts by the owner while discounting the property's connection to the taxing jurisdiction).

Through borrowing rigid, formalistic "in transit" precedents, *Harrison* and *Midland* have rejected the pragmatic approach to the Dormant Commerce Clause recognized in *Complete Auto*. The Texas Supreme Court's denial of review in these two petitions confirms that the split will not resolve itself.

C. Using older cases to inform the nexus analysis distorts the *Complete Auto* framework and warrants certiorari.

The *Complete Auto* test is this Court's general framework for analyzing taxes under the Dormant Commerce Clause. *Complete Auto* closed a schism between older cases presuming that states inherently lacked authority over interstate commerce and others holding that interstate commerce could be made to "pay its way." *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 284 (1977). It reaffirmed that there was

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at 224 ("The crude oil in the present case was not in storage but, rather, was in transit in the stream of interstate commerce."); *cf. Missouri Gas*, 234 P.3d at 955 ("Were the court making the old 'in transit' or 'at rest' determination, this record would make that determination very difficult ").

no "free trade" immunity from taxes on interstate commerce, *id.* at 278-79, and instead that taxes were permitted if they met the four requirements later termed the *Complete Auto* test, *id.* at 279.

Since 1977, that framework has been applied to many state and local taxes and regulations. The Court has developed a sophisticated set of tools for measuring discriminatory effect.

But the Court has given little guidance about how to interpret the first prong of *Complete Auto* – the "substantial nexus" prong. As a result, the lower courts are floundering. The *Harrison* and *Midland* courts' approach of using older cases to inform this analysis subverts *Complete Auto* by carving out an antique, Nineteenth Century "free trade" immunity for commerce. Just as anachronistically, these "in transit" cases embed into their analysis assumptions about what discrimination is or is not permissible – creating tension with the more evolved modern versions of the second and third prong of *Complete Auto.*[10]

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[10] For example, *Midland* justifies its adherence to the "in transit" test by noting that, otherwise, multiple states might have jurisdiction over the goods at some point in their journey *Midland*, 282 S.W.3d at 224 (citing *Michigan-Wisconsin Pipe Line Co v. Calvert*, 347 U.S. 157, 170 (1954)). But under *Complete Auto*, the second and third prongs address any multiple-taxation concern directly; there is no need to overload the first prong, which is simply the wrong tool *E.g., Oklahoma Tax Comm'n v Jefferson Lines, Inc.*, 514 U S 175, 184 (1995).

This tension between the framework used in the older cases such as *Minnesota v. Blasius*, 290 U.S. 1, 9-10 (1933) (goods in the flow of interstate commerce have "immunity . . . from state taxation"), and the *Complete Auto* framework goes back to first principles. The continuity-of-transit cases are looking for a hook to divest states of jurisdiction – movement in commerce – by elevating the goods into a special realm of federal immunity. If that hook is imported into the nexus prong of *Complete Auto*, it would sap all the flexibility and nuance from the modern test.

II. These Decisions Reflect an Untenable View of *Complete Auto*.

The Texas courts have made two related mistakes about a single prong of the *Complete Auto* test: (1) looking to whether the oil or gas was "in transit" as a measure for substantial nexus with the state and (2) framing nexus as whether the taxpayer had other "activity" in the state beyond ownership of the taxable *res*.

A. The "in transit" authorities presuppose immunity from taxation in which interstate commerce does not pay its own way.

The Texas courts focused extensively on whether the gas or oil would be considered "in transit" – and did so by invoking cases built on the pre-*Complete Auto* idea that interstate commerce was immune from

taxation. *See Harrison*, 270 S.W.3d at 215-17 (in holding the gas was "in transit," relying on Supreme Court constitutional cases from 1886, 1922, 1926, 1929, 1933, 1947, and 1954); *Midland*, 282 S.W.3d at 221-23 (adding a case from 1921).[11]

Those cases presuppose an absolute immunity of interstate commerce from state taxing authority. *E.g.*, *Blasius*, 290 U.S. at 9-10 (continuous movement creates "immunity of the property from state taxation"); *Champlain Realty*, 260 U.S. at 276 (discussing "the immunity from state taxation [of] things actually in interstate commerce").

And that stands in tension with *Complete Auto*, which acknowledged a shift away from the constitutional understanding within which those pre-*Complete Auto* cases were decided. For that reason, they do not meaningfully inform a proper evaluation of "substantial nexus" under the modern *Complete Auto* test.

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[11] *Michigan-Wisconsin Pipe Line Co. v. Calvert*, 347 U.S. 157 (1954), *Indep. Warehouses v. Scheele*, 331 U.S. 70 (1947); *Minnesota v Blasius*, 290 U.S. 1 (1933); *Carson Petroleum Co v. Vial*, 279 U.S. 95 (1929); *Hughes Bros. Timber Co v. Minnesota*, 272 U.S. 469 (1926); *Champlain Realty Co v Town of Brattleboro*, 260 U.S. 366 (1922); *Eureka Pipe Line Co. v Hallanan*, 257 U.S 265 (1921); *Coe v Errol*, 116 U.S. 517 (1886).

1. "In transit" does not fit *Complete Auto*.

The historical understanding of "in transit" cannot be imported wholesale into *Complete Auto*'s nexus prong without displacing the rest of the test. The Court stated its goal to have a "standard of permissibility of state taxation based upon its actual effect rather than its legal terminology." *Complete Auto*, 430 U.S. at 281. A return to "in transit" is a step backwards and would serve "only to distract the courts and parties from their inquiry into whether the challenged tax produced results forbidden by the Commerce Clause." *Id.* at 285.

Reviving the "in transit" test also brings back the *Spector* philosophy that "interstate commerce should enjoy a sort of 'free trade' immunity from state taxation." *Complete Auto*, 430 U.S. at 278 (discussing *Spector Motor Serv. v. O'Connor*, 340 U.S. 602 (1951)). *Complete Auto* should have dispelled those ghosts of constitutional history. Under its four-prong test, "interstate commerce may be made to pay its way." *Complete Auto*, 430 U.S. at 284-85.

2. "In transit" unduly penalizes competing intrastate commerce and would distort the market.

Natural gas is a market where the "in transit" test would put a thumb on the free-market balance

between local (intrastate) and distant (interstate) options.[12] If storage facilities along *interstate* pipelines have a federal immunity to local tax, they will have a pricing advantage over nearby sources of gas.

The Dormant Commerce Clause should level the field for interstate commerce, not award it an unearned edge in the marketplace. The market distortion caused by this holding strongly suggests that the formalistic "in transit" rule has broken with the reality of the modern economy.

B. For ad valorem property taxes, nexus should be measured against the goods, not the taxpayer.

The court of appeals based its nexus holding on a wrongly framed legal test. Instead of asking whether the goods themselves had a sufficient nexus with Texas to support a nondiscriminatory tax, it instead asked whether the taxpayer had some other *in personam* contacts beyond ownership of the goods.

The *Midland* court described this as a search for some other "activity" by the nominal owner of the oil within the borders of the state. *Midland*, 282 S.W.3d

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[12] Texas, for example, has a substantial network of purely intrastate natural-gas pipelines. *See* "Intrastate Natural Gas Segment," http://www.eia.doe.gov/pub/oil_gas/natural_gas/analysis_publications/ngpipeline/intrastate.html (visited Feb. 8, 2010) ("Intrastate pipelines in Texas account for 45,000 of the 58,600 miles of natural gas pipelines in the state.").

at 224. In a functionally similar test, *Harrison* looked for whether the taxpayer had some "personal presence" within the state beyond the presence of the natural gas. *Harrison*, 270 S.W.3d at 218. These formulations became central to each court's holding under the nexus prong.[13]

In one of the Court's few statements on the nexus prong of *Complete Auto*, it borrowed a due-process formulation saying that a tax requires substantial nexus "between a state and the person, property, or transaction it seeks to tax." *Allied-Signal, Inc. v. Director, Div. of Taxation*, 504 U.S. 768, 777 (1992) (quoting *Miller Bros. v. Maryland*, 347 U.S. 340, 344-45 (1954)). Before *Complete Auto*, the Court had stated how local ad valorem taxes can be imposed on local property: "Of course, the situs of property may tax it regardless of the citizenship, domicile, or residence of the owner." *Miller Bros.*, 347 U.S. at 345.

But the Court has not yet spoken so plainly about how the Commerce Clause gauges nexus over these same ad valorem taxes after *Complete Auto*.

In the absence of specific guidance, the lower courts now disagree about what test to use for nexus. Oklahoma looks for nexus with the property.

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[13] *Midland* acknowledged, "the oil itself had a substantial nexus with this state." 282 S.W.3d at 224. And *Harrison* noted that "[i]f one were to look strictly at the generic act of storing gas . . it might appear that such an activity would have a substantial nexus with the State." 270 S.W.3d at 218.

Missouri Gas, 234 P.3d at 955 (looking to the presence of the gas, not the taxpayer, within the state). But the Texas courts have looked for nexus with some "activity" of the out-of-state owner of the property being taxed. *Midland*, 282 S.W.3d at 224; *Harrison*, 270 S.W.3d at 218.

Looking to nexus with the owner's "activities" would lead to bizarre results for local governments who depend on ad valorem property tax. For these local taxing jurisdictions, marshaling such proof may be a challenge. Nor does distinguishing between taxable property based on whether its owner happens to have *other* activities or property nearby further the constitutional values underpinning the Commerce Clause. The Court should clearly state that nexus for ad valorem property taxes should be measured against the property being taxed, not its owner.

III. Both Petitions Warrant Attention.

With *Harrison* and *Midland*, the Court can choose between two petitions raising the same constitutional issue. In the Texas Supreme Court, these two cases were briefed in parallel and treated by the parties as intertwined.

The Court should consider taking the petitions as a pair. Failing that, it should grant a lead petition and, ultimately, vacate and remand the other.

A. The petitions offer contrasting facts that could yield a more satisfying rule than either alone.

Although both petitions involve products of the energy industry, the fact patterns differ in ways that bear on the older "in transit" analysis. As a pair, they may offer a more satisfying way to announce a rule than any single, later petition is likely to do:

(1) The *Harrison CAD v. Peoples Gas* petition presents a classic case of natural gas storage facilities, akin to a warehouse for goods. This should have passed muster even under the old "in transit" cases because the gas was stored for business reasons, such as shifting supply to meet seasonal variations in market demand.

(2) The *Midland CAD v. BP America* petition presents something more akin to a cross-dock for goods, where some oil barely pauses and other oil is subjected to "batching," "blending," and "staging" for different purposes and lasting different periods of time.[14] Although the better holding is that taxing this property satisfies *Complete Auto*, this is a closer case.

By taking this set of petitions, the Court can announce a rule that deals both with goods arguably

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[14] Even under a strict "in transit" analysis, some of these operations might interrupt the continuity of transit. For example, "blending" combines fuel with different characteristics to make a more marketable product than its original components.

"in transit" under pre-*Complete Auto* jurisprudence (such as oil in the *Midland* tank farm) and goods that are plainly "in storage" under that view (such as the gas in *Harrison*). Addressing both at once is the surest way to remove the confusion over how, if at all, these concepts fit under *Complete Auto*.

B. At a minimum, the *Midland* petition should be held for an eventual GVR.

1. A GVR would ensure the *Midland* court applies the correct rule.

The *Midland* opinion directly discussed *Harrison*, concluding that the facts in its own case "present[] an even stronger case for a Commerce Clause violation than did the circumstances in [*Harrison*]." 282 S.W.3d at 223-24.

The reason? Its reading of pre-*Complete Auto* cases about whether goods are "in transit." *Id.* at 221-22 (citing no federal cases from after 1933); *id.* at 224 (citing "in transit" as key to nexus). If the Court grants review in *Harrison* and ultimately (and correctly) reverses, then a vacatur and remand of *Midland* would permit it to apply the modern test.

2. There is little doubt that the Court has jurisdiction to GVR *Midland*.

The *Midland* opinion discusses a provision of Texas law that asks if the property being taxed was

present "for more than a temporary period." TEX. TAX CODE §21.02(a)(1); *Midland*, 282 S.W.3d at 224. Without referencing any state case law – and without even offering a construction of the statutory text – the opinion pointed back to its much more extensive discussion of federal law ("[a]s discussed above") to explain how it applied state law. *Id.* at 224-25.

As a threshold matter, a state-law ground only affects this Court's jurisdiction if its independence is "clear from the face of the opinion." *Michigan v. Long*, 463 U.S. 1032, 1040 (1983). Nowhere does the opinion state that this was an *independent* question of state law. Nor does it say that the scope of the Texas statute ("more than a temporary period") in any way departs from federal constitutional constraints. Instead of an independent state-law analysis, the opinion cross-referenced its federal holding. *Midland*, 282 S.W.3d at 224.

Second, the Court has jurisdiction whenever "a state court's interpretation of state law has been influenced by an accompanying interpretation of federal law." *Three Affiliated Tribes of Fort Berthold Reservation v. Wold Eng'g, P.C.*, 467 U.S. 138, 152 (1984). Federal law, including an extensive discussion of whether the oil was "in transit" under pre-*Complete Auto* precedents, 282 S.W.3d 221-22, drove the outcome here.

Third, although the presumptions of *Michigan v. Long* make further inquiry unnecessary, this area of

Texas law is in fact deeply "interwoven" with federal law. *Id.* at 1040.

That's because Texas pushes its taxing jurisdiction over tangible personal property to the constitutional limit; only those exemptions spelled out in the state constitution or required by conflicting federal law are permitted; mere state statutes cannot authorize exemptions.[15] *Appraisal Review Bd. v. Tex-Air Helicopters, Inc.*, 970 S.W.2d 530, 534 (Tex. 1998) (holding that another portion of this statute was permissible as "an attempt to comply with United States constitutional mandates").[16]

When a state has bound itself to an unduly limiting view of federal constraints – when driven by "what it understood to be federal constitutional considerations to construe and apply its own law in

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[15] TEX. CONST. art VIII, §1(b) ("All real and personal property in this State, unless exempt as required or permitted by this Constitution . . shall be taxed in proportion to its value"). No party has argued that these goods are exempt under any *state* constitutional provision The only possible source of exemption is federal law.

[16] In cases involving state constitutional rights, Texas courts have been instructed to make clear whenever they rely on a presumed deviation between state and federal law. *Davenport v. Garcia*, 834 S.W.2d 4, 20 (Tex 1992) (an opinion should, if appropriate, "provide a 'plain statement' that it is relying on independent and adequate state law") The *Midland* court did not There is no state constitutional exemption at issue here; only federal exemptions could apply.

the manner it did," *Zacchini v. Scripps-Howard Broad. Co.*, 433 U.S. 562, 568 (1977) – this Court is in a unique position to protect the balance of federalism by granting review.

CONCLUSION

The petition should be granted.

Respectfully submitted,

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No. 10-896

In the Supreme Court of the United States

HARRISON CENTRAL APPRAISAL DISTRICT,
Petitioner,

v.

THE PEOPLES GAS, LIGHT AND COKE COMPANY,
Respondent.

On Petition for Writ of Certiorari to the Court of Appeals of Texas, Sixth District

BRIEF OF THE TEXAS MUNICIPAL LEAGUE, THE TEXAS CITY ATTORNEYS ASSOCIATION, THE NATIONAL LEAGUE OF CITIES, THE INTERNATIONAL MUNICIPAL LAWYERS ASSOCIATION, THE NATIONAL ASSOCIATION OF TOWNS AND TOWNSHIPS, THE MICHIGAN TOWNSHIPS ASSOCIATION, THE MICHIGAN MUNICIPAL LEAGUE, THE ALABAMA LEAGUE OF MUNICIPALITIES, AND THE NEW JERSEY LEAGUE OF MUNICIPALITIES AS *AMICI CURIAE* IN SUPPORT OF PETITIONER

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INTEREST OF *AMICI CURIAE*

The *amici* submit this brief in support of Petitioner, the Harrison Central Appraisal District.[1] The Texas Municipal League (TML) is a non-profit association of more than 1,100 incorporated cities. TML provides legislative, legal, and educational services to its members. The Texas City Attorneys Association (TCAA), an affiliate of TML, is an organization of more than 400 attorneys who represent Texas cities and city officials in the performance of their duties. Other *amici* include the National League of Cities, the International Municipal Lawyers Association, the National Association of Townships and Towns, the Michigan Townships Association, the Michigan Municipal League, the Alabama League of Municipalities, and the New Jersey League of Municipalities. The *amici* collectively work to better local governments throughout the United States.

SUMMARY OF THE ARGUMENT

This case concerns when goods are constitutionally protected from ad valorem taxation under the Commerce Clause of the United States Constitution. U.S. CONST., Art. I, § 8, cls. 1 & 3. Specifically, the question presented is whether the Commerce Clause prohibits the taxation of natural gas that is stored in

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[1] In accordance with Rule 37.6, *amici* state that no counsel for a party has authored this brief, in whole or in part, and that no person or entity, other than *amici* or their members, have made a monetary contribution to the preparation or submission of this brief. Counsel of record for all parties received notice at least 10 days prior to the due date of the *amici curiae's* intention to file this brief. The parties have consented to the filing of this brief.

one state before being transferred to another state for final distribution. The resolution of this issue is of substantial importance to local governments because of the significant implications that the ad valorem taxation of natural gas could have on the budgets of these governments.

ARGUMENT

I. The dormant Commerce Clause allows the ad valorem taxation of property that is stored in the state.

The parties in this case dispute whether natural gas stored in Texas during shipment is taxable under the Commerce Clause. The Texas court of appeals held that the gas was not taxable under the United States Constitution's Commerce Clause because: (1) the goods are in transit; (2) the owner did not have a "physical presence" in Texas; (3) the owner did not have a substantial nexus to the taxing entity; and (4) the owner did not use the services of the taxing entity. To the contrary, gas stored in Texas can be constitutionally taxed by local entities. Harrison Central argued below, and in this Court, that the stored gas avails itself of the services provided by Harrison County and has a sufficient relationship to Harrison County to be taxed. Under the Court's prior cases, the gas is taxable when stored within a taxing entity. We ask this Court to review this issue to determine for this entity, and all taxing entities, as to whether property stored in a certain location, but before being transported to its final destination, may constitutionally be taxed.

Most real and personal property in Texas is taxed. The Texas Constitution provides that:

> All real property and tangible personal property in this State, unless exempt as required or permitted by this Constitution, whether owned by natural persons or corporations, other than municipal, shall be taxed in proportion to its value, which shall be ascertained as may be provided by law.

TEX. CONST. art. VIII, § 1(b). Section 11.01 of the Tax Code mirrors this language and states that, "[a]ll real and tangible personal property that this state has jurisdiction to tax is taxable unless exempt by law." TEX. TAX CODE § 11.01.

The Commerce Clause of the United States Constitution places limits on what property is taxable based on the property's relationship with the taxing entity and whether the property is in interstate commerce. The Commerce Clause states that, "[t]he Congress shall have Power . . . [t]o regulate Commerce with foreign Nations, and among the several States, and with the Indian Tribes;." U.S. CONST., ART. I, § 8, cls. 1 & 3. The "dormant Commerce Clause" prohibits a law or regulation that discriminates against interstate commerce. *Dep't of Rev. of Ky. v. Davis*, 553 U.S. 328, 338 (2008). However, "[i]t was not the purpose of the commerce clause to relieve those engaged in interstate commerce from their just share of state tax burden even though it increases the cost of doing the business." *Western Live Stock v. Bureau of Rev.*, 303 U.S. 250, 254 (1938).

The Court has interpreted the clause many times to determine whether or not property is taxable. In this case, multiple tests were used to make the underlying decision. These tests included: (1) the "continuity of transit" test from *Minnesota v. Blasius*, 290 U.S. 1 (1933) and other cases; (2) the "physical presence" requirement as discussed in the context of sales and use taxes in *Quill Corp. v. North Dakota*, 504 U.S. 298 (1992); and (3) the *Complete Auto* test from *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274 (1977). Harrison Central Appraisal District has argued that the primary test should be the four-part test in *Complete Auto*, and we agree. Further, gas stored underground meets the constitutional requirements of *Complete Auto*.

a. *Is the "continuity of transit" test still essential to dormant Commerce Clause analysis after* Complete Auto?

The "continuity of transit" test is no longer essential to dormant Commerce Clause analysis and has been superseded by *Complete Auto's* test of the taxed property's relationship with the taxing entity. *See Blasius*, 290 U.S. 1; *Complete Auto Transit, Inc.*, 430 U.S. at 279. Reviewing the issues for taxation of property in interstate commerce, the Court stated in *Blasius* that, " . . . the states may not tax property in transit in interstate commerce." *Blasius*, 290 U.S. at 9. The Court held that whether property was still in transit was a decision to be made on a case-by-case basis hinging upon whether or not the goods were still in interstate commerce or had come to rest "so that [the owner] may dispose of it either within the state, or for shipment elsewhere, as his interest dictates. . . . " *Id.* at 10-11. In contrast to that analysis, the Court in

Complete Auto disregarded the issue of whether property is "in transit" or in "interstate commerce" and instead looked at whether it made sense under the Constitution to allow a state or local entity to tax the property. 430 U.S. at 288. Interstate commerce, in and of itself, is not immune from taxation. *Id.* at 288; *see also Western Live Stock*, 303 U.S. at 254 (holding that products in interstate commerce are not immune from taxation). Because property in interstate commerce can be taxed locally, the "continuity of transit" rule that relies solely on whether a product is still moving in interstate commerce (or not) is no longer a reasonable approach to taxation of property. As noted in Harrison Central's brief, both the former Solicitor General and the Supreme Court of Oklahoma have stated that the "continuity of transit" test is no longer the appropriate inquiry. Pet. for Cert. at 14-16. We agree and would ask the Court to determine that a more comprehensive test, like that stated in *Complete Auto*, is the correct test for the constitutionality of ad valorem taxation of products that may be in transit.

b. Is the "physical presence" of the business necessary for the constitutional ad valorem taxation of personal property?

Physical presence of the property, rather than the business, should be the test for determining sufficient contacts for constitutional ad valorem taxation. Another test of whether an activity could be taxed is based on whether the owner of the property has sufficient contacts with the state through the physical presence of the business, or his agents, in the locality. *Quill Corp.*, 504 U.S. 298 (1992); *Nat'l Bellas Hess, Inc. v. Dep't of Rev. of State of Ill.*, 386 U.S. 753, 757-58 (1967). The Court stated in *Bellas Hess* that a state

cannot tax a business "whose only connection with customers in the State is by common carrier or the United States mail." *Bellas Hess*, 386 U.S. at 758. The Court emphasized that there is a difference in the ability to tax a business that has a shop or a salesman in a locality, which allows taxation, and a business that solely requests business by mail, where there would be insufficient contacts to allow taxation. *Id.* In *Quill Corp.*, the Court upheld the rule of *Bellas Hess* as it relates to sales and use taxes, but did not make a final determination as to whether the *Bellas Hess* "physical presence" rule would apply to ad valorem taxation. *Quill Corp.*, 504 U.S. at 314. "Although we have not, in our review of other types of taxes, articulated the same physical-presence requirement that *Bellas Hess* established for sales and use taxes, that silence does not imply repudiation of the *Bellas Hess* rule." *Quill Corp.*, 504 U.S. at 314. Thus, it is undecided whether "physical presence" of the property owner is necessary for an ad valorem taxation analysis. The Court's acceptance of Harrison Central's petition for certiorari would enable the Court to decide this issue and help local governments determine what property can be taxed. In doing this analysis, it makes sense to require the "physical presence" of the business for taxation when the selling of the product is being taxed because the activity being taxed is the *sales and use* of property. Similarly, it makes sense to apply the "physical presence" requirement for ad valorem taxation to the property in question because the *property itself* is what is being taxed, not the activity of the seller or owner. In the case of stored natural gas, the presence of the natural gas in the locality should be enough to meet the "physical presence" requirement. However, that would not end the inquiry.

c. *Can the natural gas stored in either an underground storage facility connected to an interstate pipeline be taxed by a state or local government under the* Complete Auto *four-part test?*

Natural gas stored in a locality before being transported to its final destination in another state has sufficient contacts to be taxable under the *Complete Auto* test. *Complete Auto* involved vehicles that were manufactured in other states and then transported to Mississippi for sale. *Complete Auto Transit, Inc. v. Brady*, 430 U.S. at 276. The tax on the vehicles was a sales tax assessed by the State of Mississippi. *Id.* at 275. The Court reviewed prior case law and stated the following test for determining the validity of the taxation:

> . . . have considered not the formal language of the tax statute but rather its practical effect, and have sustained a tax against Commerce Clause challenge when the tax is applied to an activity with a substantial nexus with the taxing State, is fairly apportioned, does not discriminate against interstate commerce, and is fairly related to the services provided by the State.

Id. at 279. The components of the *Complete Auto* test in question in this case are: (1) whether the "activity has a substantial nexus with the taxing" entity; and (2) whether the tax is "fairly related to the services provided by" the taxing entity.

Substantial Nexus

The substantial nexus requirement is similar to the physical presence requirement addressed in *Quill Corp.* and *Bellas Hess*. The purpose of the substantial nexus test is to "limit[] state burdens on interstate commerce." *Quill Corp.*, 504 U.S. at 313. No specific criteria or definition is given for "substantial nexus," but the Court has held that contact by mail or common carrier is not enough for a substantial nexus. *Nat'l Bellas Hess*, 386 U.S. at 758. The Supreme Court of Oklahoma, in a case similar to this one, discussed the substantial nexus issue as it relates to natural gas storage. *In re Assessment of Personal Property Taxes Against Missouri Gas Energy, Div. of Southern Union Co., for Tax*, 234 P.3d 938, 954-58 (Okla. 2008). The court stated that, "[u]nlike the sporadic communications with random consumers in a state deemed lacking in *National Bellas Hess*, MGEs storage gas has a substantial physical presence in the state throughout the year." *Id.* at 955. In this case, the activity and property at issue is the same, the storage of natural gas. The gas is not simply passing through the state, but is coming to rest in Harrison County to wait for distribution. A gas company that stores gas is not simply contacting individuals in a state or sending them products through the mail. Rather, it is contacting the state and county through the storage of its property. We request that the Court review this case and hold that the storage of natural gas is sufficient contact with a governmental entity to meet the substantial nexus sufficient to tax the property.

Related to Services

The "fairly related to services provided by" the taxing entity prong examines whether the taxed property or activity has enough contact with the locality to be eligible to receive services from the locality. *Complete Auto*, 430 U.S. at 279, 287; *see also Colonial Pipeline Co. v. Traigle*, 421 U.S. 100, 108-109 (1975) (holding that a franchise tax was constitutional where the activity bore a special relation to the protections and privileges provided by the taxing entity). The Court reviewed the constitutionality of a "severance" tax for coal mining in *Commonwealth Edison Co. v. Montana*, 453 U.S. 609 (1981). The Court reviewed the *Complete Auto* test and held that the tax was constitutional in part because the tax was related to the services provided by the state. *Id.* at 628-29. The Court also analyzed the issue of whether there should be a determination of the amount of the tax based on how many "services" the business was actually receiving. *Id* at 627. The ultimate conclusion was that the legislative branch should decide how much the tax should be, and the Court should decide only whether the activity's or property's relation to the taxing entity was enough to warrant the tax. *Id.* at 627-29. In the case of the coal mining, the relationship of mining the coal within the locality was sufficient. *Id.* The Supreme Court of Oklahoma held that gas storage was "fairly related to services provided by" the taxing entity in its state. *In re Assessment of Personal Property Taxes Against Missouri Gas Energy, Div. of Southern Union Co., for Tax*, 234 P.3d at 954-58. It stated that:

> The Commerce Clause does not shield property and activities connected to interstate commerce

> from having to contribute to the general cost of providing governmental services even if those costs are not readily attributable to the taxed property or activity. . . . The tax in this case operates on the presence of personal property in Woods County. It is taxed to the same extent as all other personal property in the county. MGE is therefore being asked to shoulder no more than its fair share for the support of government-provided services and the receipt of "the advantages of a civilized society."

Id. at 959 (citations omitted). In this case, the property–the natural gas–is also being stored in the taxing entity's jurisdiction. The working gas, as the pipeline terms it, is receiving the same services and protection as the cushion gas that continuously resides in the storage facility. If there is a fire, a fire truck from the locality would service the location. The public safety services, among others, are not just providing protection to the pipeline business, or to the cushion gas, but also to the working gas stored in the locality. The protections and privileges of Harrison County, the State of Texas, and other localities are offered to the property that is located in the locality, not only to the businesses that operate there. The natural gas in this case is eligible to receive the same services as any other property stored or used in the state, and should be made to pay the same burden as other taxed property. We request that the Court review this case and hold that the owners of the natural gas be required to pay the same ad valorem taxes that owners of other personal property in the state are required to pay.

II. Whether the dormant Commerce Clause allows the ad valorem taxation of property that is stored in the state needs to be decided in order to provide stability to taxation required by local governments and incurred by property owners who are engaged in interstate commerce.

In Texas, cities and counties, as well as schools, depend on ad valorem taxation to help pay for the services they provide. Almost 35% of city resources in Texas come from ad valorem taxes. "Where Do Texas Cities Get Their Money?" *Texas Town & City* January 2011 at 18, available at http://www.tml.org/legal_pdf/WhereDoCitiesGetTheirMoney.pdf. The majority of county funds in Texas also come from ad valorem taxes. *County Expenditures Survey 2010,* County Information Project, Texas Association of Counties, available at http://www.county.org/resources/countydata/products/financial/Expenditures_2010_Final.pdf. Counties and cities provide their services to everyone, including the owners of natural gas, regardless of whether the actual business is in Texas or in another state. As briefed by Harrison Central, 400 underground natural gas storage facilities operate in the United States. Thirty-four of them are in Texas. U.S. Energy Information Admin., Independent Statistics and Analysis, About U.S. Natural Gas Pipelines, Underground Natural Gas Storage, Underground Storage by U.S. Region, http://www.eia.doe.gov/pub/oil_gas/natural_gas/analysis_publications/ngpipeline/undrgrnd_storage.html (last visited Feb. 7, 2011). As stated in the underground storage report, these facilities are not simply used to transport gas but are there to provide "an inventory management tool, seasonal supply

backup, and access to natural gas needed to avoid imbalances between receipts and deliveries on a pipeline network." All taxing entities and taxed businesses need to know what can be taxed. In Oklahoma, stored gas is taxed. But in Texas it cannot be taxed. Stored gas is receiving similar government services, is being used in the same way, as described above, and touches the taxing entities in the same way. This property should be treated the same way for constitutional purposes. The Supreme Court of Oklahoma was correct when it stated that gas owners are being asked only to, "shoulder no more than its fair share for the support of government-provided services and the receipt of 'the advantages of a civilized society.'" *In re Assessment of Personal Property Taxes Against Missouri Gas Energy, Div. of Southern Union Co., for Tax*, 234 P.3d at 959. Because the stored natural gas has sufficient contacts with the locality, and receives the same services, it should be taxed the same.

CONCLUSION

Amici fully acknowledge the Constitution's protection of interstate commerce and the need to avoid multiple taxation and discriminatory taxation. But there is also the need to have each type of property share the tax burden when it has sufficient contacts with the state and receives similar services. This is true whether the property is part of intrastate commerce or if the property has a final destination in another locality. The Commerce Clause and *Complete Auto* provide an analysis that allows the Court to balance these policies. Pursuant to the Court's past Commerce Clause cases, the services provided to the property in the state, and the property being taxed, we

argue that local governments should be able to tax property that is stored in their jurisdiction. For the time the property rests in a locality, it should be required to pay for the privileges and services it receives. For the above reasons, *amici* respectfully request this Court grant Harrison Central's Petition for Writ of Certiorari.

Respectfully submitted,

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